

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2010

or

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

For the transition period from _____ to _____

Commission file number: 000-25867

NAUTILUS, INC.

(Exact name of registrant as specified in its charter)

Washington
(State or other jurisdiction of
incorporation or organization)

94-3002667
(I.R.S. Employer
Identification No.)

16400 S.E. Nautilus Drive
Vancouver, Washington 98683
(Address of principal executive offices, including zip code)
(360) 859-2900
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically a nd posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

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

Large Accelerated Filer	<input type="checkbox"/>	Accelerated Filer	<input type="checkbox"/>
Non-Accelerated Filer	<input type="checkbox"/>	Smaller Reporting Company	<input checked="" type="checkbox"/>

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

Number of shares of issuer's common stock outstanding as of October 31, 2010: 30,744,336

NAUTILUS, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2010

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PART I. FINANCIAL INFORMATION
Item 1. FINANCIAL STATEMENTS

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

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	September 30, 2010	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 14,485	\$ 7,289
Restricted cash	494	—
Trade receivables, net of allowances of \$574 as of September 30, 2010 and \$4,160 as of December 31, 2009	12,580	27,799
Inventories	11,015	13,119
Prepays and other current assets	5,274	5,097
Income taxes receivable	624	13,178
Assets of discontinued operation held-for-sale	794	10,781
Total current assets	45,266	77,263
Restricted cash	—	4,933
Property, plant and equipment, net	4,560	8,042
Goodwill	2,848	2,794
Other intangible assets, net	19,290	20,838
Other assets	1,378	1,302
Total assets	\$ 73,342	\$ 115,172
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Trade payables	\$ 18,807	\$ 37,107
Accrued liabilities	7,745	10,744
Warranty obligations, current portion	3,886	7,129
Deferred income tax liabilities	821	1,220
Total current liabilities	31,259	56,200
Long-term notes payable to a related party	5,009	—
Income taxes payable	3,015	2,866
Deferred income tax liabilities - non-current	1,341	754
Warranty obligations - non-current	1,009	1,250
Other non-current liabilities	1,519	1,619
Total liabilities	43,152	62,689
Commitments and contingencies (Note 12)		
Stockholders' equity:		
Common stock - no par value, 75,000 shares authorized, 30,744 shares issued and outstanding at September 30, 2010 and December 31, 2009	4,904	4,414
Retained earnings	18,334	41,136
Accumulated other comprehensive income	6,952	6,933
Total stockholders' equity	30,190	52,483
Total liabilities and stockholders' equity	\$ 73,342	\$ 115,172

See accompanying notes to condensed consolidated financial statements.

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

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	Three Months Ended September 30,< /div>		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net sales	\$ 38,474	\$ 41,431	\$ 114,760	\$ 135,588
Cost of sales	21,856	21,150	61,708	65,194
Gross profit	16,618	20,281	53,052	70,394
Operating expenses:				
Selling and marketing	14,347	14,278	47,935	53,202
General and administrative	4,797	5,240	14,750	18,587
Research and development	699	1,283	2,290	3,917
Restructuring	—	201	—	14,046
Asset impairment losses	—	2,101	—	2,101
Total operating expenses	19,843	23,103	64,975	91,853
Operating loss	(3,225)	(2,822)	(11,923)	(21,459)
Other income and expense:				
Interest income	4	5	15	15
Interest expense	(9)	(4)	(9)	(152)
Other income	343	858	284	476
Total other income	338	859	290	339
Loss from continuing operations before income taxes	(2,887)	(1,963)	(11,633)	(21,120)
Income tax expense (benefit)	(489)	(440)	130	505
Loss from continuing operations	(2,398)	(1,523< /font>)	(11,763)	(21,625)
Disconti nued operation:				
Loss from discontinued operation	(1,728)	(23,538)	(10,778)	(37,936)
Income tax expense (benefit) from discontinued operation	180	(643)	261	(553)
Loss from discontinued operation, net of tax	(1,908)	(22,895)	(11,039)	(37,383)
Net loss	\$ (4,306)	\$ (24,418)	\$ (22,802)	\$ (59,008)
Loss per share from continuing operations:				
Basic and diluted	\$ (0.08)	\$ (0.05)	\$ (0.38)	\$ (0.71)
Loss per share from discontinued operation:				
Basic and diluted	\$ (0.06)	\$ (0.75)	\$ (0.36)	\$ (1.22)
Net loss per share:				
Basic and diluted	\$ (0.14)	\$ (0.80)	\$ (0.74)	\$ (1.93)
Weighted average shares outstanding:				
Basic and diluted	30,744	30,681	30,744	30,637

See accompanying notes to condensed consolidated financial statements.

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

	Nine Months Ended	
	September 30,	
	2010	2009
Cash flows from operating activities:		
Loss from continuing operations	\$ (11,763)	\$ (21,625)
Loss from discontinued operation	(11,039)	(37,383)
Net loss	(22,802)	(59,008)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	5,171	8,624
Allowance for doubtful accounts	1,278	1,246
Inventory lower-of-cost-or-market adjustments	2,177	1,281
Stock-based compensation expense	490	1,219
Loss on asset disposals	144	18,334
Reduction of previously-estimated loss on disposal of commercial business	(3,156)	—
Asset impairments	—	5,124
Writeoff of abandoned leasehold improvements and other assets	—	9,516
Deferred income taxes, net of valuation allowances	372	(990)
Changes in operating assets and liabilities:		
Trade receivables	13,528	24,478
Inventories	3,694	&n bsp; 12,308
Prepaid and other current assets	1,059	192
Income taxes	12,490	11,589
Trade payables	(18,499)	(5,824)
Accrued liabilities, including warranty obligations	(5,301)	(9,027)
Net cash provided by (used in) operating activities	(9,355)	19,062
Cash flows from investing activities:		
Proceeds from sale of discontinued operation	6,930	—
Proceeds from other asset sales	16	208
Purchases of equipment	(189)	(1,808)
Decrease in restricted cash	4,439	—
Release of escrow deposit	—	2,000
Net cash provided by investing activities	11,196	400
Cash flows from financing activities:		
Net decrease in short-term borrowings	—	(17,944)
Proceeds from long-term borrowings from a related party	5,000	—
Bank financing fees	(353)	(75)
Net cash provided by (used in) financing activities	4,647	(18,019)
Net effect of currency exchange rate changes	708	22
Net increase in cash and cash equivalents	7,196	1,465
Cash and cash eq uivalents, beginning of period	7,289	5,547
Cash and cash equivalents, end of period	\$ 14,485	\$ 7,012
Supplemental disclosure of cash flow information:		
Cash refunded for income taxes	\$ 12,607	\$ 10,614
Cash paid for interest	\$ —	\$ 227

See accompanying notes to condensed consolidated financial statements.

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

(1) General Information

Basis of Consolidation and Presentation

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

The accompanying condensed consolidated financial statements have not been audited. Nautilus has condensed or omitted certain information and footnote disclosures normally included in financial statements presented in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”). Management believes the disclosures are adequate to make the information presented not misleading. However, you should read these condensed consolidated financial statements in conjunction with the Company’s consolidated financial statements and notes thereto included in its Annual Report on Form 10-K for the year ended December 31, 2009 (the “2009 Form 10-K”).

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Further information regarding significant estimates can be found in the Company’s 2009 Form 10-K.

In the opinion of management, the accompanying condensed consolidated financial statements reflect all adjustments necessary to present fairly the Company’s financial position as of September 30, 2010 and December 31, 2009, results of operations for the three and nine months ended September 30, 2010 and 2009, and cash flows for the nine months ended September 30, 2010 and 2009. Interim results are not necessarily indicative of results for a full year. The Company’s revenues typically vary seasonally and this seasonality can have a significant effect on operating results, inventory levels and working capital needs.

Unless indicated otherwise, all information regarding the Company’s operating results pertains to its continuing operations.

Liquidity

At September 30, 2010, the Company had \$14.5 million of cash and cash equivalents. Typically, the Company’s principal sources of liquidity are cash flows provided by operations. However, the Company has had continued losses since 2007 and did not generate positive cash flows from operations in the first nine months of 2010. Cash used in operating activities was \$9.4 million for the first nine months of 2010, compared to cash provided by operating activities of \$19.1 million for the first nine months of 2009 and \$14.8 million and \$5.6 million for the years ended December 31, 2009 and 2008, respectively. The Company generated positive operating cash flows despite reporting significant net losses in each of these prior periods, primarily by significantly reducing receivables and inventories.

Within the terms of its loan agreement with Bank of the West, the Company elected to uncollateralize certain standby letters of credit, which released approximately \$2.2 million of previously restricted cash in the first nine months of 2010. The Company currently is in compliance with the financial covenants of its bank loan agreement. However, there is no assurance that the Company will remain in compliance with such covenants in the future. Failure to maintain compliance with the covenants might, absent a waiver from the bank, result in an obligation to cash collateralize the Company’s standby letters of credit.

In September 2010, the Company entered into a borrowing agreement with a related party, which provided \$5.0 million in additional cash for the Company’s future operating needs. In addition, the Company completed its transition to a new primary consumer credit financing provider during the third quarter of 2010.

Management believes that sufficient funds will be available to meet the Company’s expected cash needs for at least the next twelve months, based on cash currently on hand and anticipated cash flows from operations. Despite negative operating cash flows in the first nine months of 2010, management expects to generate adequate operating cash flows during the next twelve months, primarily by reducing losses of the Company’s commercial business discontinued operation and improving contribution of its direct business through increased sales. However, there is no assurance that such funds will be sufficient for the Company’s operating needs.

New Accounting Pronouncements

No new accounting pronouncements since December 31, 2009 had, or are reasonably likely to have, a material impact on the Company's consolidated financial position, results of operations or cash flows.

Reclassifications

The results of the commercial business, including directly-related restructuring expenses, have been reclassified as discontinued operations in the Company's financial statements for all periods presented.

(2) Discontinued Operation

On September 25, 2009, in light of continuing operating losses in its commercial business and in order to focus exclusively on management of its direct and retail consumer businesses, the Company committed to a plan for the complete divestiture of its commercial business, which qualified for held-for-sale accounting treatment. The commercial business is presented as a discontinued operation in the Company's condensed consolidated statements of operations for all periods. Following is a summary of the operating results of the discontinued commercial business for the three and nine months ended September 30, 2010 and 2009 (in thousands):

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3,156

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenue	\$ 427	\$ 19,573	\$ 11,654	\$ 58,291
Operating loss before income taxes	(2,546)	(4,830)	(13,934)	(19,228)
Reduction of previously-estimated disposal loss	818	—	—	
Income tax (expense) benefit	(180)	244	(261)	154
Estimated loss on sale of commercial business	—	(18,331)	—	(18,331)
Deferred tax benefit on sale	—	399	—	399
Loss from discontinued operation - commercial business	\$ (1,908)	\$ (22,518)	\$ (11,039)	\$ (37,006)

3,156

In the third quarter and first nine months of 2010, the Company recognized reductions in the amount of pre-tax loss previously estimated in connection with the disposal of its commercial business of \$0.8 million and \$3.2 million, respectively. The following tables present gains or losses recognized on completed disposal transactions for the three and nine months ended September 30, 2010 (in thousands):

Three months ended September 30, 2010

	Previously-estimated Disposal Loss	Completed Transactions Gain (Loss)	Adjustments to Estimated Disposal Loss	Reduction of Previously- Estimated Disposal Loss
Sale of Virginia real property	\$ (1,284)	\$ (706)	\$ —	\$ 578
Other completed disposals	(184)	(472)	—	(288)
Adjustments to previously-completed disposals	—	499	—	499
Remaining assets held-for-sale as of September 30, 2010	(1,483)	—	29	29
	<u>\$ (2,951)</u>	<u>\$ (679)</u>	<u>\$ 29</u>	<u>\$ 818</u>

Nine months ended September 30, 2010

	Previously- estimated Disposal Loss	Completed Transactions Gain (Loss)	Adjustments to Estimated Disposal Loss	Reduction of Previously- Estimated Disposal Loss
Sale of commercial equipment manufacturing operation	\$ (6,212)	\$ (4,816)	\$ —	\$ 1,396
Sale of Virginia real property	(1,268)	(706)	—	562
Other completed disposals	(564)	(496)	—	68
Adjustments to previously-completed disposals	—	364	—	364
Remaining assets held-for-sale as of September 30, 2010	(2,222)	—	766	766
	<u>\$ (10,266)</u>	<u>\$ (5,654)</u>	<u>\$ 766</u>	<u>\$ 3,156</u>

Assets of discontinued operation held-for-sale and related disposal loss impairments as of September 30, 2010 were as follows (in thousands):

	Inventory	Property, Plant and Equipment	Total
Carrying value before impairment adjustment	\$ 1,241	\$ 1,008	\$ 2,249
Disposal loss impairment	(973)	(482)	(1,455)
Assets of discontinued operation held-for-sale, net	<u>\$ 268</u>	<u>\$ 526</u>	<u>\$ 794</u>

The Company expects to incur additional cash charges related to its planned divestiture of the commercial business, including estimated employee termination severance payments of approximately \$0.4 million and estimated termination charges for leases and other commercial contract obligations of approximately \$0.6 million, which have not been recognized as the related liabilities have not yet been incurred. The amounts of such additional costs in future periods may differ from these estimates depending on changes that may occur in the underlying facts and circumstances, and the amount of the difference could be material.

Fitness Apparel Business

In the fourth quarter of 2007, the Company committed to a plan to sell the operations of its fitness apparel business, which operated under the trade name Pearl iZumi. On April 18, 2008 the Company completed the sale of Pearl iZumi. The results of operations associated with Pearl iZumi's activities are included in the condensed consolidated financial statements as discontinued operations. Following is a summary of the operating results of the discontinued fitness apparel business for the three and nine months ended September 30, 2009 (in thousands):

	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2009
Revenue	<u>\$ —</u>	<u>\$ —</u>
Loss on adjustment to previously-completed disposal *	\$ (377)	\$ (377)
Income taxes	<u>—</u>	<u>—</u>
Loss from discontinued operation - fitness apparel business	<u>\$ (377)</u>	<u>\$ (377)</u>

* Reimbursement paid by the Company for expenses incurred by buyer, due under terms of the sale agreement.

(3) Restructuring Activities and Exit Costs

In the first quarter of 2009, Nautilus announced a new restructuring plan aimed at further reducing operating costs and improving the overall alignment of spending with expected revenues. The plan impacted all Company functions through personnel reductions and other cost-saving initiatives, including the discontinuation of certain product lines, the abandonment of certain information technology software and reductions in leased office space. No restructuring expenses were incurred in

the three and nine months ended September 30, 2010.

The following is a summary of restructuring expenses in the three and nine months ended September 30, 2009 (in thousands):

	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2009
Employee severance costs	\$ —	\$ 462
Abandonment of information technology software and related service agreements	—	1,799
Facility lease termination costs and other lease obligations	201	2,818
Abandonment of leasehold improvements	—	8,028
Contract termination costs	—	939
Total restructuring expense	<u>\$ 201</u>	<u>\$ 14,046</u>

The following is a summary of liabilities for exit costs, including amounts related to discontinued operations, which are included in “Accrued liabilities” and “Other non-current liabilities” in the Company’s condensed consolidated balance sheets (in thousands):

	Severance Costs	Facilities and Other Leases	Total Liabilities
Balance as of January 1, 2009	\$ 1,684	\$ —	\$ 1,684
Accruals	563	5,230	5,793
Payments	(1,884)	(3,530)	(5,414)
Balance as of December 31, 2009	363	1,700	2,063
Accruals	1,346	819	2,165
Payments	(1,168)	(827)	(1,995)
Balance as of September 30, 2010	<u>\$ 541</u>	<u>\$ 1,692</u>	<u>\$ 2,233</u>

(4) Inventories

Inventories consisted of the following at September 30, 2010 and December 31, 2009 (in thousands):

	September 30, 2010	December 31, 2009
Finished goods	\$ 9,328	\$ 11,850
Parts and components	1,687	1,269
	<u>\$ 11,015</u>	<u>\$ 13,119</u>

Inventories are stated net of valuation allowances, primarily for excess parts, of \$0.8 million at September 30, 2010 and \$0.7 million at December 31, 2009. For the three-month periods ended September 30, changes in inventory valuation allowances were not significant in 2010 and decreased cost of sales by \$0.6 million in 2009. For the nine-month periods ended September 30, changes in inventory valuation allowances were not significant in 2010 and decreased cost of sales by \$0.3 million in 2009.

(5) Property, Plant and Equipment

Property, plant and equipment consisted of the following at September 30, 2010 and December 31, 2009 (in thousands):

	Estimated useful life (in years)	September 30, 2010			December 31, 2009		
		Cost	Accumulated Depreciation	Carrying Value	Cost	Accumulated Depreciation	Carrying Value
Leasehold improvements	5 to 20	\$ 2,570	\$ (1,123)	\$ 1,447	\$ 2,767	\$ (909)	\$ 1,858
Computer equipment and software	2 to 5	39,191	(37,734)	1,457	41,225	(37,635)	3,590
Machinery and equipment	3 to 5	8,484	(7,154)	1,330	8,393	(6,823)	1,570
Furniture and fixtures	5	1,065	(889)	176	2,573	(2,103)	470
Construction in process	N/A	150	—	150	554	—	554
Total		\$ 51,460	\$ (46,900)	\$ 4,560	\$ 55,512	\$ (47,470)	\$ 8,042

(6) Goodwill and Other Intangible Assets

Goodwill and other intangible assets consisted of the following at September 30, 2010 and December 31, 2009 (in thousands):

	Estimated useful life (in years)	September 30, 2010	December 31, 2009
Goodwill	N/A	\$ 2,848	\$ 2,794
Other intangible assets:			
Indefinite life trademarks	N/A	\$ 9,052	\$ 9,052
Patents	1 to 16	18,154	18,154
Total cost		27,206	27,206
Accumulated amortization - patents		(7,916)	(6,368)
		\$ 19,290	\$ 20,838

Nautilus reviews goodwill and other indefinite-lived intangible assets for impairment in the fourth quarter of each year, or more frequently when events or changes in circumstances indicate the assets may be impaired. The change in goodwill since December 31, 2009 is due to currency exchange rate fluctuations.

(7) Product Warranties

The Company's products carry limited, defined warranties for defects in materials or workmanship which, according to their terms, generally obligate Nautilus to pay the costs of supplying and shipping replacement parts to customers and, in certain instances, pay for labor and other costs to service products. Outstanding product warranty periods range from sixty days to the lifetime of certain product components. Changes in the Company's product warranty liability for the three- and nine-month periods ended September 30, 2010 and 2009 were as follows (in thousands):

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Nine Months Ended								
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3,265								
Three Months Ended								
September 30,September 30,								
2010200920102009								
Balance at beginning of period	\$	6,258	\$	14,138	\$	8,379	\$	17,837
Accruals		361		346		1,062		
Adjustments		(525)		(1,470)		(1,245)		(1,710)
Payments		(1,199)		(2,507)		(3,301)		(8,885)
Balance at end of period	\$	4,895	\$	10,507	\$	4,895	\$	10,507

Product warranty payments and the balance outstanding at the end of each period primarily represents obligations related to the commercial business discontinued operation, for which sales volume and related product warranty expense accruals have declined significantly each year since 2007. In addition, a significant portion of product warranty payments represents obligations related to a single product of the commercial business discontinued operation for which production was ceased in 2007 and for which the related warranty expense was fully recognized in 2007 and prior.

(8) Borrowings

On December 29, 2009, the Company entered into a Letter of Credit Agreement (the “Letter of Credit Agreement”) with Bank of America (“BofA”). The Letter of Credit Agreement provides up to \$6.0 million in standby letters of credit and expires on December 31, 2010 (“Expiration Date”). BofA will issue standby letters of credit, with a maximum maturity not to exceed 365 days beyond the Expiration Date. At September 30, 2010, the Company had \$0.4 million in standby letters of credit issued under the Letter of Credit Agreement. Standby letters of credit under the Letter of Credit Agreement are secured by a cash collateral account held by BofA in an amount not less than 105% of the amount of the outstanding letters of credit.

On March 8, 2010, the Company entered into a Loan and Security Agreement (the “Loan Agreement”) with Bank of the West, providing for a \$15.0 million maximum revolving secured credit line. The amount available for borrowings in any given quarter is dependent upon the amount of qualified accounts receivable and inventory as of the end of the preceding quarter. The Loan Agreement is available for working capital, standby letters of credit and general corporate purposes through August 2012, assuming the Company satisfies certain terms and conditions at the time borrowings are requested. The interest rate on any future borrowings under the Loan Agreement will be based on the bank’s prime rate or LIBOR and the Company’s financial condition at the time it elects to borrow. The Loan Agreement includes a fee for the unused portion of the credit facility, which will vary depending on the Company’s borrowing base availability.

The Loan Agreement is collateralized by substantially all of the Company’s assets and contains customary covenants, including minimum current ratio, minimum liquidity, minimum EBITDA and limitations on capital expenditures, mergers and acquisitions, indebtedness, liens, dispositions, dividends and investments. The Loan Agreement also contains customary events of default. Upon an event of default, the lender would have the option of accelerating all obligations under the Loan Agreement. Standby letters of credit under the Loan Agreement are treated as a reduction of the Company’s available borrowing base and are subject to covenant testing. If standby letters of credit are secured by a cash collateral account held by Bank of the West in an amount not less than 105% of the amount of the outstanding letters of credit and there are no outstanding borrowings under the Loan Agreement, then covenant testing is not applicable.

In the third quarter of 2010, the Company completed amendments to the Loan Agreement which specify separate, more lenient financial covenants, compliance with which permits the Company to maintain outstanding standby letters of credit without a requirement for cash collateral. The amendment to the Loan Agreement restricts the Company’s ability to borrow under the Loan Agreement absent compliance with the pre-amendment covenants. The separate financial covenants are applicable for compliance measurement periods through March 31, 2011. The Loan Amendment also required the Company to obtain \$5 million of unsecured indebtedness, subordinated to the Loan Agreement, as additional working capital on or before September 16, 2010. The Company obtained this indebtedness on September 3, 2010.

At September 30, 2010, the Company had no outstanding borrowings and \$3.8 million in standby letters of credit under the Loan Agreement. At September 30, 2010, the Company was in compliance with the financial covenants; however there is no assurance that the Company would be in compliance with the financial covenants in the foreseeable future such that it could access the credit facility if the need were to arise or, absent a waiver from the bank, avoid cash collateralizing its outstanding letters of credit.

On September 3, 2010, the Company entered into a Note Purchase Agreement (the “Purchase Agreement”) by and among Nautilus and certain entities (collectively, the “Purchasers”) under common control of Sherborne Investors GP, LLC and its affiliates (collectively “Sherborne”). Sherborne is the Company’s largest shareholder and is controlled by Edward J. Bramson, the Company’s Chairman and Chief Executive Officer, and Craig L. McKibben, a member of the Company’s Board of Directors.

Pursuant to the Purchase Agreement, the Company issued to the Purchasers \$6,096,996 in aggregate principal amount at maturity of its Increasing Rate Senior Discount Notes Due December 31, 2012 (the “Notes”). The Notes have an original principal amount totaling \$5,000,000 and mature on December 31, 2012. The then outstanding principal amount of the Notes accretes value at rates equal to 2.5% per annum from September 3, 2010 through February 28, 2011; 6.0% per annum from March 1, 2011 through August 31, 2011; 9.5% per annum from September 1, 2011 through February 29, 2012; 13.0% per annum from March 1, 2012 through August 31, 2012; and 14.5% per annum thereafter. If all the Notes are paid at maturity, the effective rate of interest is 8.7% per annum. Prepayment of amounts due under the Notes is permitted under the Purchase Agreement.

The Notes are subordinated to the Loan Agreement with Bank of the West. The Purchase Agreement includes certain negative covenants, including restrictions on the incurrence of additional indebtedness, liens, liquidation of assets, capital expenditures, changes in the Company’s business operations and change of control transactions. The Purchase Agreement includes customary

events of default, including nonpayment, insolvency breach of warranty or covenant, cross-default of the Loan Agreement, material adverse changes, and other events. Upon the occurrence of an event of default the Purchasers may declare all outstanding obligations under the Notes to be due and payable. The accretion rate of the Notes is increased by 2% per annum during the continuance of an event of default.

(9) Loss Per Share

Basic loss per share is calculated based on the weighted-average number of common shares outstanding during the period. Diluted loss per share is calculated based on the weighted-average number of common shares outstanding, after giving effect to the potential dilution that could occur upon exercise of dilutive securities, as determined using the treasury stock method.

Following is a calculation of basic and diluted loss per share for the three and nine months ended September 30, 2010 and 2009 (in thousands, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Numerator:				
Loss from continuing operations	\$ (2,398)	\$ (1,523)	\$ (11,763)	\$ (21,625)
Loss from discontinued operation	(1,908)	(22,895)	(11,039)	(37,383)
Net loss	<u>\$ (4,306)</u>	<u>\$ (24,418)</u>	<u>\$ (22,802)</u>	<u>\$ (59,008)</u>
Denominator:				
Basic and diluted shares outstanding	<u>30,744</u>	<u>30,681</u>	<u>30,744</u>	<u>30,637</u>
Calculations:				
Loss per share from continuing operations - basic and diluted	\$ (0.08)	\$ (0.05)	\$ (0.38)	\$ (0.71)
Loss per share from discontinued operation - basic and diluted	<u>\$ (0.06)</u>	<u>\$ (0.75)</u>	<u>\$ (0.36)</u>	<u>\$ (1.22)</u>
Net loss per share - basic and diluted	<u>\$ (0.14)</u>	<u>\$ (0.80)</u>	<u>\$ (0.74)</u>	<u>\$ (1.93)</u>

Potentially dilutive average shares of 1.2 million and 1.7 million for the three months ended September 30, 2010 and 2009, respectively, were not included in the computation of diluted loss per share because they would have been antidilutive, reducing the amount of loss per share. Potentially dilutive average shares of 1.3 million and 1.8 million for the nine months ended September 30, 2010 and 2009, respectively, were not included in the computation of diluted loss per share because they would have been antidilutive, reducing the amount of loss per share.

(10) Comprehensive Loss

Following is a summary of the components of comprehensive loss, net of income taxes, for the three and nine months ended September 30, 2010 and 2009 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net loss	\$ (4,306)	\$ (24,418)	\$ (22,802)	\$ (59,008)
Foreign currency translation adjustments	(620)	582	19	545
Comprehensive loss	<u>\$ (4,926)</u>	<u>\$ (23,836)</u>	<u>\$ (22,783)</u>	<u>\$ (58,463)</u>

(11) Reportable Segments and Related Information

The Company has two reportable segments: Direct and Retail, each representing a distinct marketing distribution channel. The Company's direct business offers its products directly to consumers in the United States and Canada through direct-response advertising, catalogs and the Internet. The Company's retail business offers its products for resale to consumers through a network of third-party retailers located in the United States and internationally, as well as Internet-based merchants. The Company's commercial business is reported as a discontinued operation and is not a reportable segment. Contribution is the measure of profit or loss used by the Company's chief operating decision maker, and is defined as net sales, less product costs

and operating expenses directly attributable to the segment. Segment operating expenses include employment costs, selling and marketing expenses, general and administrative expenses and research and development expenses solely related to direct and retail business unit operations. Restructuring expenses are unallocated to allow for better comparisons of segment operating results among periods. Summary information by operating segment for the three and nine months ended September 30, 2010 and 2009 is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net sales:				
Direct	\$ 21,504	\$ 25,253	\$ 68,450	\$ 94,169
Retail	16,118	15,656	43,869	39,560
Unallocated corporate (royalty income)	852	522	2,441	1,859
Consolidated net sales	<u>\$ 38,474</u>	<u>\$ 41,431</u>	<u>\$ 114,760</u>	<u>\$ 135,588</u>
Contribution:				
Direct	\$ (2,686)	\$ 1,740	\$ (9,200)	\$ 5,055
Retail	2,001	2,229	5,594	4,803
Unallocated corporate	854	249	2,443	891
Consolidated contribution	<u>\$ 169</u>	<u>\$ 4,218</u>	<u>\$ (1,163)</u>	<u>\$ 10,749</u>
Reconciliation of consolidated contribution to loss from continuing operations:	< /td>			
Consolidated contribution	\$ 169	\$ 4,218	\$ (1,163)	\$ 10,749
Less unallocated corporate expenses:	< font style="font-family:inherit;font-size:10pt;">			
Selling and marketing	—	(300)	—	(875)
General and administrative	(3,394)	(4,037)	(10,696)	(13,911)
Research and development	—	(401)	(64)	(1,275)
Restructuring	—	(201)	—	(14,046)
Intangible asset impairment charge	—	(2,101)	—	(2,101)
Other income	338	859	290	339
Income taxes	489	440	(130)	(505)
Loss from continuing operations	<u>\$ (2,398)</u>	<u>\$ (1,523)</u>	<u>\$ (11,763)</u>	<u>\$ (21,625)</u>

(12) Commitments and Contingencies

Legal Matters

The Company is party to various legal proceedings arising from normal business activities. In addition, the Company's tax filings are subject to audit by authorities in the jurisdictions where it conducts business, which may result in assessments of additional taxes. Management believes it has adequately provided for obligations that would result from these legal and tax proceedings where it is probable the Company will pay some amount and such amount can be reasonably estimated. In some cases, however, it is too early to predict a final outcome. Management believes that the ultimate resolution of these matters will not have a material effect on the Company's financial position, results of operations or cash flows.

Guarantees, Commitments and Off-Balance Sheet Arrangements

The Company purchases the products it sells from third-party manufacturers, mainly located in Asia. In August 2010, the Company completed an amendment to its agreement with its largest supplier, which extends the term of the agreement through December 31, 2011. The Company has long lead times for inventory purchases and therefore needs to secure factory capacity from its suppliers in advance. At September 30, 2010, the Company had approximately \$12.6 million in non-cancellable market-based purchase obligations, all of which were for inventory purchases expected to be received during the remainder of 2010.

Prior to its divestiture, the Company's discontinued commercial business would, from time-to-time, involve a third-party with lease and financing arrangements to assist customers in purchasing products. While these financings generally were without

recourse to Nautilus, in certain cases the Company offered a guarantee or other recourse provisions. At September 30, 2010, the maximum potential liability under all outstanding recourse provisions was approximately \$1.0 million. The Company is not aware of any circumstances or events that have occurred for which it would be liable under such provisions.

At September 30, 2010, the Company had \$4.3 million in outstanding standby letters of credit expiring through September 2011.

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

The following discussion and analysis is based upon our financial statements as of the dates and for the periods presented in this section. You should read this discussion and analysis in conjunction with the financial statements and notes thereto found in Item 1 of this Form 10-Q and our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2009 (the "2009 Form 10-K"). All references to the third quarters of 2010 and 2009 mean the three-month periods ended September 30, 2010 and 2009, respectively. Unless the context otherwise requires, "Nautilus," "we," "us" and "our" refer to Nautilus, Inc. and its subsidiaries. Unless indicated otherwise, all information regarding our operating results pertains to our continuing operations.

Our results of operations may vary significantly from period-to-period. Our revenues will fluctuate due to the seasonality of our industry; customer buying patterns; product innovation; the nature and level of competition for health and fitness products; our ability to procure products to meet customer demand; and the level of spending on, and effectiveness of, our media and advertising programs. In addition, our operating results are highly susceptible to the availability of consumer credit, both in the U.S. and Canada, the overall condition of the U.S. economy and economies of other countries where we market our products, by fluctuations in the costs or availability of materials used to manufacture our products, changes in fuel prices, changes in the cost of distribution or other services, variations in our product sales mix and the relative success of strategies we employ to improve the efficiency and effectiveness of our organization. Historically, our operating expenses have been influenced by media costs to produce and broadcast our advertisements, facility costs, operating costs of our information and communications systems, costs to develop and maintain our Internet websites, bad debt expenses, costs related to attracting and retaining key personnel, asset impairment losses and restructuring charges.

As a result of the above and other factors, our period-to-period operating results may not be indicative of our future performance. You should not place undue reliance on our operating results and should consider our prospects in light of the risks, expenses and difficulties typically encountered by us and other companies, both within and outside our industry, in the current and expected future economic environments. We may not be able to successfully address these risks and difficulties and, consequently, we cannot assure you of any future growth or profitability. For more information, see our discussion of *Risk Factors* located at Part I, Item 1A of our 2009 Form 10-K.

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Forward-Looking Statements

This Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "plan," "expect," "aim," "believe," "project," "intend," "estimate," "will," "should," "could," and other terms of similar meaning typically identify forward-looking statements. The forward-looking statements in this Form 10-Q include, without limitation, statements regarding improved availability of consumer credit for our customers through our new primary consumer credit financing provider, our plans and expectations regarding borrowing agreements, our new product development strategies and our plans for achieving future profitability. Forward-looking statements also include any statements related to our expectations regarding future business and financial performance or conditions, anticipated sales growth across markets, distribution channels and product categories, expenses and gross margins, timing and availability of consumer credit financing offered through third parties, expense as a percentage of revenue, profits or losses, new product introductions, capital expenditures, cost reduction plans, financing and working capital requirements and resources. These forward-looking statements, and others we make from time to time, are subject to a number of risks and uncertainties. Many factors could cause actual results to differ materially from those projected in forward-looking statements, including the risks described in Part I, Item 1A, "Risk Factors," in our 2009 Form 10-K, as supplemented or amended by our quarterly reports on Form 10-Q, which are incorporated herein by reference. We do not undertake any duty to update forward-looking statements after the date they are made or to conform them to actual results or to changes in circumstances or expectations.

Available Information

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports, available free of charge on our website. In addition, our code of business conduct and ethics, corporate

governance policies, and the charters of our Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee are available on our corporate website. The information presented on our website is not part of this report.

Overview

Nautilus is a fitness products company providing innovative, quality solutions to help people achieve a fit and healthy lifestyle. We are a leading designer, developer and marketer of fitness products sold around the world. We believe our brands are some of the strongest in the industry. We market our products through two business segments: direct and retail. Our direct business offers products directly to consumers in the United States and Canada through direct-response advertising, catalogs and the Internet. Our retail business offers our products for resale to consumers through a network of third-party retailers located in the United States and internationally, as well as Internet-based merchants.

During the third quarter of 2009, we committed to a plan for the complete divestiture of our commercial business with the expectation that successful completion of this plan would improve our overall operating results. Consequently, our commercial business has been classified as a discontinued operation. Our commercial business offered products to health clubs, schools, hospitals and other organizations. The disposition of most commercial business assets has been completed and we expect to dispose of the remaining assets over the remainder of this year.

Now we are focusing our resources exclusively on supplying fitness equipment to consumers through our direct and retail sales channels, which we believe offer the best prospects for achieving profitability in the future. We will continue to invest in new product development when opportunities arise for us to bring new and innovative products to consumers. Currently, our new product development efforts focus on three key areas of physical fitness and personal health: strength, cardio and stretching, and aim to deliver to customer expectations of simplicity, efficient results and space considerations - all at an affordable price. Our new product development strategies leverage our existing strong array of brands and internally-developed features and innovations, as well as the potential acquisition of third-party technologies.

Net sales of our direct business decreased 14.8% in the third quarter of 2010, compared to the third quarter of 2009, primarily due to a 35% year-over-year decrease in the rate of customer credit approvals by our primary third-party consumer credit financing provider during the respective periods, which was partially offset by financing approvals from our new secondary third - party provider. Gross profit margin of our direct business decreased by 7.7 percentage points in the third quarter of 2010, compared to the third quarter of 2009, primarily due to increased sales discounts.

Net sales of our retail business increased 3.0% in the third quarter of 2010, compared to third quarter of 2009, primarily due to customer demand for our newly-redesigned fitness bikes and sales to new customers. Gross profit margin of our retail business decreased by 2.2 percentage points in the third quarter of 2010, compared to the third quarter of 2009, primarily due to lower pricing on excess stocks of treadmills. Higher retail gross profit margin in the third quarter last year also was attributable to adjustments to previously-recognized reserves for warranty costs.

Loss from continuing operations was \$2.4 million in the third quarter of 2010, an increase in loss of \$0.9 million, compared to a loss of \$1.5 million in the third quarter of 2009. Loss from continuing operations in the third quarter 2009 included a pre-tax asset impairment charge of \$2.1 million related to an intangible asset of our retail business and \$0.2 million in restructuring expenses. Our results for the third quarter of 2010 were favorably impacted by reductions in general & administrative and research & development costs. The favorable impact of these operating cost reductions was more than offset, however, by lower sales and reduced gross margin in our direct business.

We believe that a major challenge facing our direct business is the availability of financing to our customers from our third-party consumer credit financing providers. Our third-party consumer credit financing providers offer revolving credit arrangements to qualified customers of our direct business in order to finance their purchases. The third-party financing provider determines when to approve financing, as well as the timing of payments, interest rate, fees and other terms and conditions of the customer's credit account. The third-party financing provider is the sole owner of the customer's credit account, which is without recourse to Nautilus in the event the account becomes uncollectible, except in limited circumstances, such as fraud. In June 2010, we entered into an agreement with a secondary third-party consumer credit financing provider to offer financing to customers with respect to credit applications which have been declined by our primary consumer credit financing provider. In September 2010, we completed our transition to a new primary third-party consumer financing provider, which management expects will result in the improved availability of credit for customers of our direct business, which should lead to increased sales in our direct business. Currently, management expects incremental growth in customer credit approval rates in the fourth quarter of 2010, as the new program with our primary third-party consumer financing provider is further optimized.

In September 2010, we completed a loan transaction with certain entities under common control of Sherborne Investors GP, LLC and its affiliates, a related party, which provided \$5.0 million in additional cash for our future operating needs.

We purchase the products we sell from third-party manufacturers, mainly located in Asia. In August 2010, we completed an amendment to our agreement with our largest supplier, which extends the term of the agreement through December 31, 2011.

COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2010 and 2009

The tables below set forth selected financial information derived from our condensed consolidated financial statements. The discussion that follows should be read in conjunction with our condensed consolidated financial statements and the related notes. All comparisons to prior year results are in reference to continuing operations only in each period, unless otherwise indicated.

	<i>(In thousands)</i>			
	Three Months Ended September 30,			
	2010	2009	\$ Change	% Change
Net sales	\$ 38,474	\$ 41,431	\$ (2,957)	(7.1)%
Cost of sales	21,856	21,150	706	3.3 %
Gross profit	16,618	20,281	(3,663)	(18.1)%
Operating expenses:				
Selling and marketing	14,347	14,278	69	0.5 %
General and administrative	4,797	5,240	(443)	(8.5)%
Research and development	699	1,283	(584)	(45.5)%
Restructuring	—	201	(201)	(100.0)%
Asset impairment losses	—	2,101	(2,101)	(100.0)%
Total operating expenses	19,843	23,103	(3,260)	(14.1)%
Operating loss	(3,225)	(2,822)	(403)	14.3 %
Other income and expense:				
Interest income	4	5	(1)	(20.0)%
Interest expense	(9)	(4)	(5)	125.0 %
Other income	343	858	(515)	(60.0)%
Total other income	338	859	(521)	(60.7)%
Loss from continuing operations before income taxes	(2,887)	(1,963)	(924)	47.1 %
Income tax benefit	(489)	(440)	(49)	11.1 %
Loss from continuing operations	(2,398)	(1,523)	(875)	57.5 %
Loss from discontinued operation, net of tax	(1,908)	(22,895)	20,987	(91.7)%
Net loss	\$ (4,306)	\$ (24,418)	\$ 20,112	(82.4)%

Direct business

Net sales of our direct business were \$21.5 million in the third quarter of 2010, a decrease of \$3.7 million, or 14.8%, compared to direct net sales of \$25.3 million in the third quarter of 2009. The comparative decrease in direct net sales was attributable primarily to a 35% year-over-year decrease in the rate of customer credit approvals by our primary third-party consumer credit financing provider during the respective periods, which was partially offset by financing approvals from our new secondary third-party provider.

In September 2010, we completed our transition to a new primary third-party consumer financing provider to address a significant decline in customer credit approval rates from our former primary third-party consumer financing provider. Currently, management expects incremental growth in customer credit approval rates in the fourth quarter of 2010 and in 2011, as the new program with our primary third-party consumer financing provider is further optimized.

Gross profit margin of our direct business was 55.1% in the third quarter of 2010, a decrease of 7.7 percentage points compared to the third quarter of 2009. The comparative decrease in direct gross profit margin was attributable primarily to increased sales discounts as we tested market reaction to various levels of pricing in certain product lines and increased promotional pricing in certain strength products. Currently, management expects to continue significant levels of promotional pricing, principally with respect to certain strength products, in the fourth quarter of 2010.

Retail business

Net sales of our retail business were \$16.1 million in the third quarter of 2010, an increase of \$0.5 million, or 3.0%, compared to retail net sales \$15.7 million in the third quarter of 2009. The increase in retail net sales was attributable primarily to customer demand for our newly-redesigned fitness bikes and sales to new customers.

Gross profit margin of our retail business was 24.4% in the third quarter of 2010, a decrease of 2.2 percentage points compared to the third quarter of 2009, primarily due to lower pricing on excess stocks of treadmills. Higher retail gross profit margin in the third quarter last year was also attributable to adjustments to previously-recognized reserves for warranty costs.

Operating expenses in the third quarter of 2010 were \$19.8 million, a decrease of \$3.3 million, or 14.1%, compared to the third quarter of 2009, primarily due to an impairment loss of \$2.1 million in the third quarter of 2009 in connection with an intangible asset of our retail business and approximately \$1.0 million in reduced operating costs resulting from cost-saving initiatives.

Selling and marketing expenses were \$14.3 million in the third quarter of 2010, an increase of \$0.1 million, or 0.5%, compared to the third quarter of 2009. Advertising expense of our direct business in the third quarter of 2010 was \$8.4 million, a decrease of \$0.4 million, or 4.5%, compared to the third quarter of 2009. The comparative decrease in direct advertising expenses primarily was attributable to management's decision to reduce television media spending until credit programs through our new primary consumer credit financing provider became available late in the third quarter of 2010, partially offset by increased media production costs. We expect to begin increasing advertising expenditures in the fourth quarter of 2010 and in 2011.

General and Administrative

General and administrative expenses were \$4.8 million in the third quarter of 2010, a decrease of \$0.4 million, or 8.5%, compared to the third quarter of 2009, primarily due to cost-saving initiatives aimed at reductions in personnel, occupancy cost, insurance expense and outside services costs.

Research and Development

Research and development expenses were \$0.7 million in the third quarter of 2010, a decrease of \$0.6 million, or 45.5%, compared to the third quarter of 2009, primarily due to personnel reductions undertaken as part of our cost-saving initiatives.

Restructuring

No restructuring costs were incurred in the third quarter of 2010. In the third quarter of 2009, restructuring expenses were \$0.2 million, consisting of additional lease terminations costs related to a reduction of leased office space in our Vancouver, Washington headquarters building.

Asset Impairment Losses

No asset impairment losses were incurred in the third quarter of 2010. In the third quarter of 2009, we recognized an impairment loss of \$2.1 million for an intangible asset of our retail business.

Other income and expense

Interest expense

In the third quarter of 2009, we incurred a nominal amount of interest in connection with our prior bank financing agreement. We repaid all amounts outstanding under our prior financing agreement in December 2009, and have not borrowed under our current financing agreement with Bank of the West. In the third quarter of 2010, we incurred a nominal amount of interest expense in connection with long-term notes payable to a related party.

Other Income

Other income was \$0.3 million in the third quarter of 2010, a decrease of \$0.5 million compared to other income of \$0.9 million in the third quarter of 2009, primarily due to a decrease in foreign currency exchange gain.

Income Tax Benefit

Income tax benefit was \$0.5 million in the third quarter of 2010, compared to a benefit of \$0.4 million in the third quarter of 2009. Income tax benefit in the third quarter of 2010 primarily relates to an income tax refund claim filed in the period.

We increased our valuation allowance in the third quarters of 2010 and 2009 to reduce U.S. deferred income tax assets generated during the respective periods to their anticipated net realizable value. As a result, we recognized only modest U.S. income tax benefits associated with our operating losses in the third quarters of 2010 and 2009.

Discontinued Operation

In connection with the exit from our commercial business, we recorded a loss from discontinued operation, net of income taxes, of \$1.9 million in the third quarter of 2010, compared to a loss of \$22.9 million in the third quarter of 2009. Loss from discontinued operations for the third quarter of 2010 is net of a \$0.8 million reduction in the amount of disposal loss previously estimated in connection with the divestiture of our commercial business.

COMPARISON OF OPERATING RESULTS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010 and 2009

The tables below set forth selected financial information derived from our condensed consolidated financial statements. The discussion that follows should be read in conjunction with our condensed consolidated financial statements and the related notes. All comparisons to prior year results are in reference to continuing operations only in each period, unless otherwise indicated.

	<i>(In thousands)</i>			
	Nine Months Ended September 30,			
	2010	2009	\$ Change	% Change
Net sales	\$ 114,760	\$ 135,588	\$ (20,828)	(15.4)%
Cost of sales	61,708	65,194	(3,486)	(5.3)%
Gross profit	53,052	70,394	(17,342)	(24.6)%
Operating expenses:				
Selling and marketing	47,935	53,202	(5,267)	(9.9)%
General and administrative	14,750	18,587	(3,837)	(20.6)%
Research and development	2,290	< font style="font-family:inherit;font-size:10pt;">3,917	(1,627)	(41.5)%
Restructuring	—	14,046	(14,046)	(100.0)%
Asset impairment losses	—	2,101	(2,101)	(100.0)%
Total operating expenses	64,975	91,853	(26,878)	(29.3)%
Operating loss	(11,923)	(21,459)	9,536	(44.4)%
Other income and expense:				
Interest income	15	15	—	— %
Interest expense	(9)	(152)	143	(94.1)%
Other income	284	476	(192)	(40.3)%
Total other income	290	339	(49)	(14.5)%
Loss from continuing operations before income taxes	(11,633)	(21,120)	9,487	(44.9)%
Income tax expense	130	505	(375)	(74.3)%
Loss from continuing operations	(11,763)	(21,625)	9,862	(45.6)%
Loss from discontinued operation, net of tax	(11,039)	(37,383)	26,344	(70.5)%
Net loss	\$ (22,802)	\$ (59,008)	\$ 36,206	(61.4)%

	<i>(In thousands)</i>			
	Nine Months Ended September 30,			
	2010	2009	\$ Change	% Change
Net sales:				
Direct business	\$ 68,450	\$ 94,169	\$ (25,719)	(27.3)%
Retail business	43,869	39,560	4,309	10.9 %
Unallocated corporate (royalty income)	2,441	1,859	582	31.3 %
Total net sales	\$ 114,760	\$ 135,588	\$ (20,828)	(15.4)%
Gross profit:				
Direct business	\$ 39,352	\$ 58,025	\$ (18,673)	(32.2)%
Retail business	11,256	11,478	(222)	(1.9)%
Unallocated corporate	2,444	891	1,553	174.3 %
Total gross profit	\$ 53,052	\$ 70,394	\$ (17,342)	(24.6)%
Gross profit margin (% of net sales):				
Direct business	57.5%	61.6%	(4.1)	% points
Retail business	25.7%	29.0%	(3.3)	% points
Total gross profit margin	46.2%	51.9%	(5.7)	% points

Direct business

Net sales of our direct business were \$68.5 million for the nine months ended September 30, 2010, a decrease of \$25.7 million, or 27.3%, compared to direct net sales of \$94.2 million for the nine months ended September 30, 2009. The comparative decrease in direct net sales was attributable primarily to a 38% year-over-year decrease in the rate of customer credit approvals by our primary third-party consumer credit financing provider during the respective periods, which was partially offset by financing approvals from our new secondary third-party provider.

In September 2010, we completed our transition to a new primary third-party consumer financing provider to address a significant decline in customer credit approval rates from our former primary third-party consumer financing provider. Currently, management expects incremental growth in customer credit approval rates in the fourth quarter of 2010 and in 2011, as the new program with our primary third-party consumer financing provider is further optimized.

Gross profit margin of our direct business was 57.5% for the nine months ended September 30, 2010, a decrease of 4.1 percentage points compared to the nine months ended September 30, 2009. The comparative decrease in direct gross profit margin was attributable primarily to increased sales discounts, as well as lower sales volume.

Retail business

Net sales of our retail business were \$43.9 million for the nine months ended September 30, 2010, an increase of \$4.3 million, or 10.9%, compared to retail net sales of \$39.6 million for the nine months ended September 30, 2009. The increase in retail net sales was attributable primarily to customer demand for our newly-redesigned fitness bikes and elliptical products and sales to new customers.

Gross profit margin of our retail business was 25.7% for the nine months ended September 30, 2010, a decrease of 3.3 percentage points compared to the nine months ended September 30, 2009. Higher gross profit margin in the first nine months last year was attributable primarily to adjustments to previously-recognized reserves for warranty and freight costs.

Operating Expenses

Operating expenses for the nine months ended September 30, 2010 were \$65.0 million, a decrease of \$26.9 million, or 29.3%, compared to the nine months ended September 30, 2009, primarily due to \$14.0 million in expenses associated with restructuring activities and an impairment loss of \$2.1 million for an intangible asset of our retail business in the first nine months of 2009. Cost saving initiatives, as well as reduced selling and marketing costs as we continued to better align those expenses with expected revenue, contributed to a decrease in operating expenses in the first nine months of 2010 of approximately \$10.7 million, or 14.2%, compared to the first nine months of 2009.

Selling and Marketing

Selling and marketing expenses were \$47.9 million for the nine months ended September 30, 2010, a decrease of \$5.3 million, or 9.9%, compared to the nine months ended September 30, 2009. Advertising expense of our direct business for the nine months ended September 30, 2010 was \$31.0 million, a decrease of \$2.6 million, or 7.8%, compared to the nine months ended September 30, 2009. The comparative decrease in advertising expense of our direct business primarily was attributable to management's decision to reduce television media spending in order to balance the ability to convert customer leads into sales in the current environment, where advertising fees have increased over the same period last year while consumer financing approval rates have declined substantially. In addition, bad debt expense decreased by \$0.5 million and third-party consumer credit financing fees decreased by \$0.5 million, primarily due to a reduction in the amount of sales financed by our third-party consumer financing providers. Combined, cost-saving initiatives and lower sales volumes reduced selling and marketing expenses by approximately \$1.7 million in the first nine months of 2010, compared to the first nine months of 2009.

General and Administrative

General and administrative expenses were \$14.8 million for the nine months ended September 30, 2010, a decrease of \$3.8 million, or 20.6%, compared to the nine months ended September 30, 2009, primarily due to cost-saving initiatives aimed at reductions in personnel, occupancy cost, insurance expense and outside services costs. In addition, general and administrative expenses for the nine months ended September 30, 2009 were reduced by the resolution of legal matters, which were settled for \$1.0 million less than the amounts previously estimated.

Research and Development

Research and development expenses were \$2.3 million for the nine months ended September 30, 2010, a decrease of \$1.6 million, or 41.5%, compared to the nine months ended September 30, 2009, primarily due to personnel reductions undertaken as part of our cost-saving initiatives.

Restructuring

No restructuring costs were incurred for the nine months ended September 30, 2010. For the nine months ended September 30, 2009, restructuring expense included an \$8.0 million impairment charge for abandoned leasehold improvements in space we are no longer using at our Vancouver, Washington headquarters facility; \$2.8 million in facility lease termination costs and other lease obligations associated with the reduction of leased space at our headquarters facility and our vacated manufacturing and distribution facilities in Tulsa, Oklahoma; \$1.8 million in charges due to our abandonment of information technology software; contract termination costs of \$0.9 million related to a warehouse distribution service agreement for our U.S. parts; and \$0.5 million in severance costs related to personnel reductions.

Asset Impairment Losses

No asset impairment losses were incurred in the first nine months of 2010. In the first nine months of 2009, we recognized an impairment loss of \$2.1 million for an intangible asset of our retail business.

Other income and expense

Interest expense

We incurred interest expense of \$0.2 million in the nine months ended September 30, 2009 in connection with our prior bank financing agreement. We repaid all amounts outstanding under our prior financing agreement in December 2009, and have not borrowed under our current financing agreement with Bank of the West. We incurred a nominal amount of interest in the nine months ended September 30, 2010 in connection with long-term notes payable to a related party.

Other Income

Other income was \$0.3 million for the nine months ended September 30, 2010, a decrease of \$0.2 million compared to other income of \$0.5 million for the nine months ended September 30, 2009, primarily due to a decrease in foreign currency exchange gain.

Income Tax Expense

Income tax expense was \$0.1 million for the nine months ended September 30, 2010, compared to \$0.5 million for the nine months ended September 30, 2009. Income tax expense primarily relates to taxable income generated outside of the United States. Income tax expense decreased in the first nine months of 2010, compared to the same period last year, primarily due to a tax refund claim of \$0.4 million filed in the third quarter of 2010.

We increased our valuation allowance for the nine months ended September 30, 2010 and 2009 to reduce U.S. deferred income tax assets generated during the respective periods to their anticipated net realizable value. As a result, we did not recognize U.S. income tax benefits associated with our operating losses in those periods.

Discontinued Operation

In connection with the exit from our commercial business, we recorded a loss from discontinued operation, net of income taxes, of \$11.0 million for the nine months ended September 30, 2010, compared to a loss of \$37.4 million for the nine months ended September 30, 2009. Loss from discontinued operations for the nine months ended September 30, 2010, is net of a \$3.2 million reduction in the amount of disposal loss previously estimated in connection with the divestiture of our commercial business.

LIQUIDITY AND CAPITAL RESOURCES

In summary, our cash flows were as follows (in thousands):

	Nine Months Ended September 30,	
	2010	2009
Net cash provided by (used in) operating activities	\$ (9,355)	\$ 19,062
Net cash provided by investing activities	11,196	400
Net cash provided by (used in) financing activities	4,647	(18,019)

At September 30, 2010, we had \$14.5 million of cash and cash equivalents. Typically, our principal sources of liquidity are our cash flows provided by our operations. However, we have had continued losses since 2007 and did not generate positive cash flows from operations in the first nine months of 2010. Cash used in operating activities was \$9.4 million for the first nine months of 2010, compared to cash provided by operating activities of \$19.1 million for the first nine months of 2009 and \$14.8 million and \$5.6 million for the years ended December 31, 2009 and 2008, respectively. We generated positive operating cash flows despite reporting significant net losses in each of these prior periods, primarily by significantly reducing trade receivables and inventories.

The economy's impact on our operating results, especially the impact of decreased availability of credit for our customers, has been worse than we anticipated. While the restructuring strategies we implemented in recent years have resulted in substantial cost savings, they have not offset the full impact of the poor economic conditions and our decline in revenues. As a result of these and other factors, we cannot project when or if we might become profitable. Our return to profitability is dependent on numerous factors, including: improved global economic conditions, particularly in the U.S.; relaxed credit markets, including improved availability of credit for our customers; resumed growth in consumer spending on discretionary goods; increased consumer confidence; and our continued execution of cost reduction initiatives. In light of the aforementioned uncertainties, there can be no assurance that we will be able to generate sufficient positive cash flows in the future.

Within the terms of our loan agreement with Bank of the West, we elected to uncollateralize certain standby letters of credit, which released approximately \$2.2 million of previously restricted cash in the first nine months of 2010. Currently we are in compliance with the financial covenants of our bank loan agreement. However, there is no assurance that we will remain in compliance with such covenants in the future. Failure to maintain compliance with the covenants might, absent a waiver from the bank, result in an obligation to cash collateralize our standby letters of credit.

In September 2010, we completed a borrowing agreement with certain entities under common control of Sherborne Investors GP, LLC and its affiliates, a related party, which provided \$5.0 million in additional cash for our future operating needs. In addition, we completed our transition to a new primary third-party consumer credit financing provider during the third quarter of 2010, which management expects will result in the improved availability of credit for our customers, which should lead to increased sales in our direct business.

Management believes that sufficient funds will be available to meet our expected cash needs for at least the next twelve months, based on cash currently on hand and anticipated cash flows from operations. Despite negative operating cash flows in the first nine months of 2010, management expects to generate adequate operating cash flows during the next twelve months, primarily by reducing losses of our commercial business discontinued operation and improving contribution of our direct business through increased sales. However, there is no assurance that such funds will be sufficient for our operating needs.

Cash used in operating activities of \$9.4 million in the first nine months of 2010 consisted primarily of losses from continuing and discontinued operations, as adjusted for non-cash items, and reductions in trade payables and accrued liabilities of \$18.5 million and \$5.3 million, respectively, partially offset by \$13.5 million from the reduction of trade receivables, \$12.5 million from income tax refunds and \$3.7 million from the reduction of inventories. Significant reductions in trade receivables, trade payables and accrued liabilities in the first nine months of 2010 largely resulted from winding down our commercial business discontinued operation. We expect further reductions in accrued liabilities in future periods as we fulfill outstanding liabilities, including product warranty obligations, of our commercial business discontinued operation.

Cash provided by operating activities of \$19.1 million in the first nine months of 2009 consisted primarily of significant reductions in trade receivables and inventories of \$24.5 million and \$12.3 million, respectively, as we reduced working capital invested in our commercial business, which was classified as a discontinued operation in the third quarter of 2009, partially offset by losses from continuing and discontinued operations, as adjusted for non-cash items, and a \$9.0 million reduction in accrued liabilities. The reduction in accrued liabilities largely results from the fulfillment of outstanding product warranty obligations of our commercial business discontinued operation, particularly a commercial treadclimber product which was discontinued in early 2008.

The following table presents comparative cash flows related to trade receivables and inventories for the nine months ended September 30, 2010 and 2009 (in thousands):

Nine Months Ended September 30,			
	2010	2009	Change
Trade receivables:			
Collections	\$ 139,942	\$ 218,357	\$ (78,415)
Sales on account	(126,414)	(193,879)	67,465
Net cash provided	<u>\$ 13,528</u>	<u>\$ 24,478</u>	<u>\$ (10,950)</u>
Inventories:			
Shipments	\$ 55,917	\$ 80,661	\$ (24,744)
Purchases	(52,223)	(68,353)	16,130
Net cash provided	<u>\$ 3,694</u>	<u>\$ 12,308</u>	<u>\$ (8,614)</u>

Cash provided by investing activities of \$11.2 million in the first nine months of 2010 included \$6.9 million in proceeds from the sale of portions of our discontinued commercial business and \$4.4 million from a reduction in the amount of restricted cash collateralizing our outstanding letters of credit. Cash provided by investing activities of \$0.4 million in the first nine months of 2009 included \$2.0 million from the release of an escrow deposit and \$0.2 million in proceeds from sales of equipment, partially offset by \$1.8 million used for purchases of equipment.

Cash provided by financing activities of \$4.6 million in the first nine months of 2010 consisted of \$5.0 million in long-term borrowings from a related party, partially offset by \$0.4 million in financing costs related to our bank loan agreement and long-term borrowings. Cash used in financing activities of \$18.0 million in the first nine months of 2009 consisted of repayments of borrowings under our former bank agreement, which was fully repaid in December 2009.

Financing Arrangements

On December 29, 2009, we entered into a Letter of Credit Agreement (the “Letter of Credit Agreement”) with Bank of America (“BoFA”). The Letter of Credit Agreement provides up to \$6.0 million in standby letters of credit and expires on December 31, 2010 (“Expiration Date”). BoFA will issue standby letters of credit, with a maximum maturity not to exceed 365 days beyond the Expiration Date. At September 30, 2010, we had \$0.4 million in standby letters of credit issued under the Letter of Credit Agreement. Standby letters of credit under the Letter of Credit Agreement are secured by a cash collateral account held by BoFA in an amount not less than 105% of the amount of the outstanding letters of credit.

On March 8, 2010, we entered into a Loan and Security Agreement (the “Loan Agreement”) with Bank of the West, providing for a \$15.0 million maximum revolving secured credit line. The amount available for borrowings in any given quarter is dependent upon the amount of qualified accounts receivable and inventory as of the end of the preceding quarter. The Loan Agreement is available for working capital, standby letters of credit and general corporate purposes through August 2012, assuming we satisfy certain terms and conditions at the time borrowings are requested. The interest rate on any future borrowings under the Loan Agreement will be based on the bank's prime rate or LIBOR and our financial condition at the time we elect to borrow. The Loan Agreement includes a fee for the unused portion of the credit facility, which will vary depending on our borrowing base availability.

The Loan Agreement is collateralized by substantially all of our assets and contains customary covenants, including minimum current ratio, minimum liquidity, minimum EBITDA and limitations on capital expenditures, mergers and acquisitions, indebtedness, liens, dispositions, dividends and investments. The Loan Agreement also contains customary events of default. Upon an event of default, the lender would have the option of accelerating all obligations under the Loan Agreement. Standby letters of credit under the Loan Agreement are treated as a reduction of our available borrowing base and are subject to covenant testing. If standby letters of credit are secured by a cash collateral account held by Bank of the West in an amount not less than 105% of the amount of the outstanding letters of credit and there are no outstanding borrowings under the Loan Agreement, then covenant testing is not applicable.

In the third quarter of 2010, we completed amendments to the Loan Agreement which specify separate, more lenient financial covenants, compliance with which permits us to maintain outstanding standby letters of credit without a requirement for cash collateral. The amendment to the Loan Agreement restricts our ability to borrow under the Loan Agreement absent compliance

with the pre-amendment covenants. The separate financial covenants are applicable for compliance measurement periods through March 31, 2011. The Loan Amendment also required us to obtain \$5 million of unsecured indebtedness, subordinated to the Loan Agreement, as additional working capital on or before September 16, 2010. We obtained this indebtedness on September 3, 2010.

At September 30, 2010, we had no outstanding borrowings and \$3.8 million in standby letters of credit under the Loan Agreement. At September 30, 2010, we were in compliance with the financial covenants; however, there is no assurance that we would be in compliance with the financial covenants in the foreseeable future such that we could access the credit facility if the need were to arise or, absent a waiver from the bank, avoid cash collateralizing our outstanding letters of credit.

On September 3, 2010, we entered into a Note Purchase Agreement (the “Purchase Agreement”) by and among Nautilus and certain entities (collectively, the “Purchasers”) under common control of Sherborne Investors GP, LLC and its affiliates (collectively “Sherborne”). Sherborne is our largest shareholder and is controlled by Edward J. Bramson, our Chairman and Chief Executive Officer, and Craig L. McKibben, a member of our Board of Directors.

Pursuant to the Purchase Agreement, we issued to the Purchasers \$6,096,996 in aggregate principal amount at maturity of its Increasing Rate Senior Discount Notes Due December 31, 2012 (the “Notes”). The Notes have an original principal amount totaling \$5,000,000 and mature on December 31, 2012. The then outstanding principal amount of the Notes accretes value at rates equal to 2.5% per annum from September 3, 2010 through February 28, 2011; 6.0% per annum from March 1, 2011 through August 31, 2011; 9.5% per annum from September 1, 2011 through February 29, 2012; 13.0% per annum from March 1, 2012 through August 31, 2012; and 14.5% per annum thereafter. If all the Notes are paid at maturity, the effective rate of interest is 8.7% per annum. Prepayment of amounts due under the Notes is permitted under the Purchase Agreement.

The Notes are subordinated to the Loan Agreement with Bank of the West. The Purchase Agreement includes certain negative covenants, including restrictions on the incurrence of additional indebtedness, liens, liquidation of assets, capital expenditures, changes in our business operations and change of control transactions. The Purchase Agreement includes customary events of default, including nonpayment, insolvency breach of warranty or covenant, cross-default of the Loan Agreement, material adverse changes, and other events. Upon the occurrence of an event of default the Purchasers may declare all outstanding obligations under the Notes to be due and payable. The accretion rate of the Notes is increased by 2% per annum during the continuance of an event of default. We agreed to indemnify the Purchasers for losses or liabilities arising out of the transactions contemplated by the Purchase Agreement.

Off-Balance Sheet Arrangements

In the past, our discontinued commercial business would, from time-to-time, involve a third-party with lease and financing arrangements to assist customers in purchasing our products. While most of these financings were without recourse to Nautilus, in certain cases we offered a guarantee or other recourse provisions. At September 30, 2010 and December 31, 2009, the maximum contingent liability under all outstanding recourse provisions was approximately \$1.0 million and \$1.4 million, respectively.

Commitments and Contingencies

For a description of our commitments and contingencies, refer to Note 12 to the condensed consolidated financial statements in Item 1.

Seasonality

We expect our sales of fitness equipment products to vary seasonally. Sales are typically strongest in the first and fourth quarters, and are generally weakest in the second quarter. We believe the broadcast of national network season finales and seasonal weather patterns influence television viewership and cause our television commercials on national cable television to be less effective in the second quarter than in other periods of the year. In addition, during the spring and summer months, consumers tend to be more involved in outdoor activities, including exercise, which impacts sales of fitness equipment used indoors. This seasonality can have a significant effect on our operating results, inventory levels and working capital needs.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our critical accounting policies have not changed from those discussed in our 2009 Form 10-K.

NEW ACCOUNTING PRONOUNCEMENTS

No new accounting pronouncements since December 31, 2009 had, or are reasonably likely to have, a material impact on our consolidated financial position, results of operations or cash flows.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We have established a system of disclosure controls and procedures that is designed to ensure that information relating to the Company, which is required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 (“Exchange Act”), is recorded, processed, summarized and reported within the time periods specified by the SEC’s rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), as appropriate to allow timely decisions regarding required disclosure. An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) was performed as of the end of the period covered by this Form 10-Q. This evaluation was performed under the supervision and with the participation of management, including our CEO and CFO. Based upon that evaluation, our CEO and CFO have concluded that these disclosure controls and procedures were effective as of the end of the period covered by this Form 10-Q.

Changes in Internal Controls over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the nine months ended September 30, 2010, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

For a description of the legal proceedings that affect us, refer to Note 12 to the condensed consolidated financial statements in Part I, Item 1.

Item 1A. Risk Factors

Nautilus operates in an environment that involves a number of risks and uncertainties. The risks and uncertainties described in our 2009 Form 10-K are not the only risks and uncertainties we face. Additional risks and uncertainties that presently are not considered material or not known to us, and therefore not mentioned herein, may impair our business operations. If any of the risks described in our 2009 Form 10-K and below actually occur, our business, operating results and financial position could be harmed. Other than the additional risk factors set forth below, there has not been a material change to the risk factors as set forth in our 2009 Form 10-K.

Our inventory purchases are subject to long lead times, which could negatively impact our sales, cash flows and liquidity.

Lead times for inventory purchases from our Asian suppliers, from order placement to receipt of goods, range from approximately two to three months, of which period transit time represents approximately three weeks. The length of our lead times requires us to place advance manufacturing orders based on management forecasts of future demand for our products. Due to the length of our lead times, our sales and cash flows may be negatively impacted if we do not have sufficient product quantities on hand to meet customer demand for such items. In addition, our liquidity and cash flows may be negatively affected, and inventory obsolescence may increase, if the quantity of products we order exceeds customer demand for such items.

We may become subject to delisting proceedings, which would have an adverse impact on the liquidity and market price of our common stock and could negatively impact our supplier and customer relationships.

Our common stock is currently traded on the New York Stock Exchange (the “NYSE”). The NYSE’s continued listing criteria require that listed companies maintain either an average global market capitalization of not less than \$50 million over a consecutive 30 trading-day period, or total stockholders’ equity of not less than \$50 million. On September 23, 2010, we were notified by the NYSE staff that we are not in compliance with this requirement for continued listing. Under applicable NYSE procedures, on October 29, 2010, we submitted to the NYSE a plan to demonstrate our ability to regain compliance with the

continued listing standards within an 18-month period. The NYSE has 45 days to accept or reject our plan. A delisting of our common stock could negatively impact us by, among other factors, reducing the volume of trading in our common stock and the number of investors willing or able to hold or acquire our common stock, damaging our reputation and standing with suppliers, lenders, customers and sources of consumer financing programs.

Item 6. Exhibits

The following exhibits are filed herewith.

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<u>Exhibit No.</u>	<u>Description</u>
10.1	Addendum dated August 20, 2010 to Supply Agreement dated May 2, 2008 between Nautilus, Inc., Treuriver Investments LIMITED, and Land America Health and Fitness Co. Ltd.
10.2	Note Purchase Agreement dated September 3, 2010, by and among Nautilus, Inc. and certain entities under common control of Sherborne Inv estors GP, LLC and its affiliates.
10.3	Subordination Agreement dated September 3, 2010, by and among Nautilus, Inc., certain entities under common control of Sherborne Investors GP, LLC and its affiliates and Bank of the West.
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14 (a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14 (a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to Rule 13a-14(b) of the Securities and Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

NAUTILUS, INC.

November 8, 2010
Date

By: /s/ Edward J. Bramson
Edward J. Bramson
Chairman and Chief Executive Officer
(Principal Executive Officer)

November 8, 2010
Date

By: /s/ Kenneth L. Fish
Kenneth L. Fish
Chief Financial Officer
(Principal Financial Officer)

**Addendum dated August 20, 2010 to Supply Agreement dated May 2, 2008 between Nautilus, Inc., Treuriver Investments LIMITED,
and Land America Health and Fitness Co. Ltd.**

This Addendum to the Supply Agreement (hereinafter “Addendum”), dated August 20, 2010 and effective January 1, 2011, supplements and amends the Supply Agreement dated May 2, 2008 (her einafter “Supply Agreement”) as hereinafter set forth and according to the following terms:

Article 1 Definitions:

The definition of “New Products” is eliminated.
< /div>

Article 3 Price:

The Preamble in Article 3 is eliminated in its entirety and replaced with the following: “The per unit purchase price payable by Purchaser to Suppliers for each Product purchased hereunder is set forth in a confidential memorandum that has been approved and agreed upon by the Parties in connection with the negotiation of this Addendum (the “Unit Price Schedule”). The Prices set forth in the Unit Price Schedule attached as Exhibit A to this Addendum shall be valid and remain in effect for all shipments made during the term of the Addendum.”

Article 3.1 shall be eliminated in its entirety.

Article 3.2 shall be eliminated in its entirety.

Article 3.3 shall be eliminated in its entirety:

Article 5 Volume Guarantees:

Article 5 is eliminated in its entirety.

Article 7 Payment:

Article 7.1: The second complete sentence of Article 7.1 shall be eliminated and replaced with the following sentence: “Beginning January 1, 2011, payment terms are net forty five (45) days and effective July 1, 2011 payment terms are net sixty (60) days and due on the Thursday of the week following the due date of the invoice, and absent a dispute regarding the amount of an invoice or an amount otherwise due under this Agreement.”

Article 7.2: Eliminate Article 7.2 in its entirety and replace it with the following: “In the event Purchaser fails to make timely full payment for undisputed product shipped between January 1, 2011 and June 30, 2011 within fifty five (55) days following the due date of the invoice in Article 7.1 (and for product shipped between July 1, 2011 and December 31, 2011 seventy (70) days following the due date of the invoice in Article 7.1), Supplier may thereafter, upon providing prior written notice to Purchaser, suspend further shipments of product until all payments are brought current. All late payments as defined in this Article will accrue interest at the rate of LIBOR plus 3% per annum until paid.”

Article 8 Certain Agreements Regarding Products:

Article 8.5: A new Article 8.5 shall be added as follows:

Suppliers agree to provide to Purchaser a full cost detailed Bill of Materials (“CBOM”) as set forth in this Article. In the event that Suppliers in the future request a price increase on any of the products on the Unit Price Schedule, Suppliers agree to provide Purchaser a CBOM for any of those products on which a price increase is being requested before any price increase goes into effect. In the event that Purchaser requests a quote from Suppliers on any Products not on the Unit Price Schedule, Suppliers agree to provide a CBOM at the time it provides the quote to Purchaser.

Article 9 Quality

Article 9.3: Eliminate Article 9.3 in its entirety and replace it with the following: “If the inspection reject rate (arising solely from inspections occurring at Supplier's facility in Xiamen, China) of a single Product reaches an unacceptable level (which shall occur if five percent (5%) or more of the Products produced within a given purchase order are rejected by Purchaser for non-conformance), Purchaser may recommend or institute corrective action.”

Article 19 Non-Competition

The amount of \$10 million USD referred to in Article 19 for the purchase of rod based home gyms shall be changed to \$6 million USD of rod based home gyms. In all other respects the terms of Article 19 remain.

Article 20 Duration of Agreement

Article 20: Substitute the date of “December 31, 2011” in place of “ December 31, 2010.”

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In all other respects the Supply Agreement dated May 2, 2008 shall remain in full force and effect through December 31, 2011.

PURCHASER:

NAUTILUS, INC.

By: /s/ William McMahon
Signature
Print Name: William McMahon
Title: SVP Consumer

Suppliers:

Treuriver Investments LIMITED

By: /s/ Michael Carmen Bruno
Signature
Print Name: Michael Carmen Bruno
Title: CEO

**LAND AMERICA HEALTH AND
FITNESS CO., LTD.**

By: /s/ Michael Carmen Bruno
Signature
Print Name: Michael Carmen Bruno
Title: CEO

Acknowledged and Agreed as to Article 19 above:

/s/ Michael Carmen Bruno
MICHAEL BRUNO

/s/ Yang Lin Qing
YANG LIN QING

NOTE PURCHASE AGREEMENT

by and among

NAUTILUS, INC.

and

THE PURCHASERS IDENTIFIED ON

ANNEX A ATTACHED HERETO

September 3, 2010

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NOTE PURCHASE AGREEMENT

\$6,096,996.21 Aggregate Principal Amount At Maturity of

Notes of the Issuers

Due December 31, 2012

THIS NOTE PURCHASE AGREEMENT (this “ Agreement ”), dated as of September 3, 2010, is by and among Nautilus, Inc., a Washington corporation (“ Nautilus ”), and the note purchasers that are now and hereafter at any time parties hereto and are listed in Annex A (or any amendment or supplement thereto) attached hereto (each, a “ Purchaser ” and, collectively, “ Purchasers ”). Capitalized terms used and not defined elsewhere in this Agreement are defined in Article 1 hereof.

RECITALS

A. Nautilus has proposed selling the Notes to Purchasers on the Closing Date in the aggregate principal amount at maturity of \$6,096,996.21 (\$5.0 million of gross proceeds to Nautilus) to provide for working capital, capital expenditures and other general corporate purposes of Nautilus.

B. Purchasers are willing to purchase such Notes from Nautilus upon the terms and subject to the conditions set forth herein.

NOW, THEREFORE, the parties hereto, in consideration of the premises and their mutual covenants and agreements herein set forth and intending to be legally bound hereby, covenant and agree as follows:

ARTICLE 1

DEFINITIONS

1.1 Certain Definitions . In addition to other words and terms defined elsewhere in this Agreement, the following words and terms have the meanings set forth below (and such meanings shall be equally applicable to both the singular and plural form of the terms defined, as the context may require):

“ Accounts ” shall mean all accounts (as defined in RCW 62A.9A-102(a)(2) (or any successor statute)) of the Issuers.

“ Accreted Value ” means, as of any date (the “ Specified Date ”), the amount provided below for each \$1,000 principal amount at maturity of the Notes.

Note Purchase Agreement

(1) if the Specified Date occurs on one of the following dates (each, an “ Accrual Date ”), the Accreted Value will equal the amount set forth below for such Accrual Date:

<u>Accrual Date</u>	<u>Accreted Value</u>
February 28, 2011	\$ 830.16
August 31, 2011	\$ 855.06
February 29, 2012	\$ 895.68
August 31, 2012	\$ 953.90
December 31, 2012	\$ 1,000.00

(2) if the Specified Date occurs before the first Accrual Date, the Accreted Value will equal the sum of (A) the original issue price of the Notes and (B) an amount equal to the product of (x) the Accreted Value for the first Accrual Date less such original issue price multiplied by (y) a fraction, the numerator of which is the number of days from the Closing Date to the Specified Date, using a 360-day year of twelve 30-day months, and the denominator of which is the number of days elapsed from the Closing Date to the first Accrual Date, using a 360-

day year of twelve 30-day months;

(3) if the Specified Date occurs between two Accrual Dates, the Accreted Value will equal the sum of (A) the Accreted Value for the Accrual Date immediately preceding such Specified Date and (B) an amount equal to the product of (x) the Accreted Value for the immediately following Accrual Date less the Accreted Value for the immediately preceding Accrual Date multiplied by (y) a fraction, the numerator of which is the number of days from the immediately preceding Accrual Date to the Specified Date, using a 360-day year of twelve 30-day months, and the denominator of which is 180; or

(4) if the Specified Date occurs after December 31, 2012, the Accreted Value will equal \$1,000.

“Affiliate” shall mean as to any Person (a) that directly or indirectly controls, is controlled by, or is under common control with any of the Issuers; provided that, Affiliate will not include Persons that would otherwise be Affiliates solely because of common control by any of the Nautilus' shareholders if such Persons are portfolio companies independently operated by such shareholders, (b) that directly or indirectly owns or holds 10 percent or more of any class of voting stock of any Issuer, or (c) 10 percent or more of the voting stock of which is directly or indirectly owned or held by any Issuer. The term “control” means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a Person, whether through the ownership of voting securities or interests, by contract, or otherwise.

“Agreement” shall mean this Note Purchase Agreement, as the same may be amended, restated, supplemented or otherwise modified from time to time.

“Bankruptcy Code” shall mean the Federal Bankruptcy Reform Act of 1978 (11 U.S.C. §101, et seq.), as amended and in effect from time to time, and the regulations issued from time to time thereunder.

“Business” shall have the business of designing, developing, sourcing and marketing cardiovascular and strength fitness products and related accessories for consumer home use, primarily in the United States and Canada.

Note Purchase Agreement

“Business Day” shall mean any day other than a Saturday, Sunday or other day on which banking institutions in New York, New York are authorized or required by law to close.

“Capital Expenditures” shall mean, with respect to any measurement period in question, all capital expenditures of the Issuers (including, but not limited to, expenditures under Capital Leases), as determined in accordance with GAAP.

“Capital Expenditure Limitation” shall have the meaning assigned to such term in Section 7.2(l) hereof.

“Capital Lease” shall mean any lease of property (real, personal, or mixed) that in accordance with GAAP should be capitalized on the lessee's balance sheet.

“Capital Stock” shall mean, with respect to any Person, all (a) shares, interests, participations or other equivalents (howsoever designated) of capital stock and other equity or ownership interests of such Person and (b) rights (other than debt securities convertible into capital stock or other equity interests), warrants or options to acquire any such capital stock or other equity interests.

“Change in Control” shall mean that (a) a majority of the directors of Nautilus shall be Persons other than Persons (i) for whose election proxies shall have been solicited by the board of directors of Nautilus or for whose appointment or election is otherwise approved or ratified by the board of directors of Nautilus or (ii) who are then serving as directors appointed by the board of directors to fill vacancies on the board of directors caused by death or resignation (but not by removal) or to fill newly-created directorships or (b) any “person” or “group” (as such terms are used in Section 13(d) of the Securities Exchange Act of 1934) becomes the “beneficial owner” (as defined in Rules 13d-3 and 13d-5 under the Securities Exchange Act of 1934, except that a person or group shall be deemed to have “beneficial ownership” of all securities that such person or group has the right to acquire whether such right is immediately exercisable or only after the passage of time), directly or indirectly, of Voting Stock of Nautilus (or other securities convertible into such Voting Stock) representing 35 percent or more of the combined voting power of all Voting Stock of Nautilus (provided that any Voting Stock held by Sherborne shall be excluded from calculation for the purposes of this clause (b)).

“Closing” shall mean the closing of the purchase and sale of the Notes pursuant to this Agreement.

“Closing Date” shall mean the date on which all conditions precedent set forth in Article 4 are satisfied or waived by all Purchasers.

“Code” shall mean the Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder.

“Confidential Information” shall have the meaning assigned to such term in Section 9.17 hereof.

“Consumer Protection Laws” shall mean any and all applicable federal, state, and local statutes, laws, regulations, rules, and ordinances (whether now existing or hereafter enacted or promulgated), and all applicable judicial, administrative, and regulatory decrees, judgments, and orders, including common law rulings and determinations, relating to consumer credit or the protection of consumers, including, but not limited to, the Consumer Credit Protection Act.

“Continuing Business Net Income” means, for any measurement period in question, the net income of Issuers arising from the Business for such period, determined in accordance with GAAP, but in any event the following items shall be excluded or deducted from such net income arising from the Business: (a) any after tax gain or loss resulting from dispositions of assets outside of the ordinary course of business, (b) earnings of any Subsidiary accrued prior to the date it became a Subsidiary, (c) any deferred credit or other credit representing any excess of the equity of any Subsidiary at the date of acquisition thereof over the amount invested in such Subsidiary, (d) the net earnings of any entity (other than a Subsidiary) in which the Issuers have an ownership interest, except to the extent such net earnings actually shall have been received by the Issuers in the form of cash distributions, (e) any reversal of a contingency reserve, except to the extent that the Issuers received cash associated with such reversal during the period in which the reversal occurred, and (f) to the extent not included in clauses (a) through (e) above, any extraordinary or non-recurring gains or losses.

“Contractual Obligations” means, as to any Person, any provision of any security issued by such Person or of any agreement, undertaking, contract, indenture, mortgage, deed of trust or other instrument, document or agreement to which such Person is a party or by which it or any of its Property is bound.

“Debt to Tangible Net Worth” shall mean, as of any date in question, the ratio of (a) total Indebtedness on the balance sheet of any Issuer to (b) the fair market value of all assets on the balance sheet of any Issuer except for (i) goodwill, including any amounts representing the excess of the purchase price paid for assets or stock acquired over the value assigned thereto on the balance sheet of any Issuer, (ii) patents, trademarks, trade names, copyrights and other intellectual property, (iii) shares of Capital Stock of any Issuer, (iv) loans and notes receivable from officers, employees, stockholders, or directors of any Issuer or any Affiliate or Subsidiary of any Issuer, (v) deferred expenses, and (v i) any other intangible asset of any Issuer that should be classified as such on the balance sheet of any Issuer in accordance with GAAP, less all liabilities on the balance sheet of any Issuer.

“Default” shall mean any event or circumstance which, with the giving of notice, the lapse of time, or both, would (if not cured or otherwise remedied during such time) constitute an Event of Default.

“Dollars”, “dollars” and “\$” each shall mean lawful money of the United States of America.

“Domestic Subsidiary” shall mean, with respect to any Person, a Subsidiary of such Person, which Subsidiary is incorporated or otherwise organized under the laws of a state of the United States of America.

“Eligible Commercial Accounts Receivable” shall have the meaning given to such term in the Senior Credit Agreement.

“Eligible Consumer Finance Accounts Receivable” shall have the meaning given to such term in the Senior Credit Agreement.

“Environmental Laws” shall mean any and all applicable federal, state, and local environmental, health, or safety statutes, laws, regulations, rules, and ordinances (whether now existing or hereafter enacted or promulgated), and all applicable judicial, administrative, and regulatory decrees, judgments, and orders, including common law rulings and determinations, relating to injury to, or the protection of, human health or the environment, including, without limitation, all requirements pertaining to reporting, licensing, permitting, investigation, remediation, and

removal of emissions, discharges, releases, or threatened releases of Hazardous Materials into the environment, or relating to the manufacture, processing, distribution, use, treatment, storage, disposal, transport, or handling of such Hazardous Materials.

“ ERISA ” shall mean The Employee Retirement Income Security Act of 1974 and the rules and regulations thereunder, collectively, as the same from time to time may be supplemented or amended and remain in effect.

“ Event of Default ” shall mean any of the events of default described in Section 8.1 hereof.

“ Excluded Tax ” means with respect to any Purchaser (a) taxes imposed on or measured by its overall net income (however denominated), and franchise taxes imposed on it (in lieu of net income taxes), in each case imposed on any Purchaser as a result of a present or former connection between such Purchaser and the jurisdiction of the Governmental Authority imposing such tax or any political subdivision or taxing authority thereof or therein (other than such connection arising solely from any Purchaser having executed, delivered, become a party to, or performed its obligations or received a payment under, or enforced or received a security interest under, the Purchase Documents); (b) any branch profits taxes imposed by the United States or any similar tax imposed by any other jurisdiction in which any Purchaser is located; (c) (i) taxes that are directly attributable to the failure (other than as a result of a change in any requirement of law rule, regulation or treaty or in the administration, interpretation or application thereof by any Governmental Authority) by any Purchaser to deliver the documentation required to be delivered pursuant to Section 3.6(f) and (ii) withholding taxes to the extent that the obligation to withhold amounts existed on the date that such Person became a “Purchaser” under this Agreement in the capacity under which such Person makes a claim under subsection 3.6(b), except in each case to the extent such Person is a direct or indirect assignee of any other Purchaser that was entitled, at the time the assignment to such Person became effective, to receive additional amounts under subsection 3.6(b); and (d) any United States federal withholding tax that would not have been imposed but for a failure by such recipient (or any financial institution through which any payment is made to such recipient) to comply with the applicable requirements of FATCA.

“ FATCA ” means sections 1471, 1472, 1473 or 1474 of the Code and the United States Treasury Regulations or published guidance with respect thereto.

“ Federal Reserve Board ” means the Board of Governors of the Federal Reserve System, or any entity succeeding to any of its principal functions.

“ Fiscal Year ” or “ fiscal year ” shall mean each 12-month period ending on December 31st of each year.

“ Funded Indebtedness ” means, on the measurement date in question, without duplication, (a) Indebtedness for borrowed money, (b) Indebtedness in respect of Capital Leases, (c) all obligations of the Person in question in respect of letters of credit, (d) all other interest-bearing obligations of the Person in question that, in accordance with GAAP, should be included as a liability on the consolidated balance sheet of the Person in question, and (e) all Guaranties executed with respect to any of the obligations described in items (a) through (d) of this definition.

“ GAAP ” shall mean the generally accepted accounting principles issued by the American Institute of Certified Public Accountants in effect in the United States at the time of application to the provisions of this Agreement.

“ Government Approval ” means an approval, permit, license, authorization, certificate, or consent of any Governmental Authority.

“ Governmental Authority ” shall mean the government of the United States, or any state or any foreign country or any political subdivision of any thereof, or any branch, department, agency, instrumentality, court, tribunal, or regulatory authority that constitutes a part of or exercises any sovereign power of any of the foregoing.

“ Guaranties ” means all guaranties, endorsements (other than endorsements of negotiable instruments for collection in the ordinary course of business), or other contingent or surety liabilities with respect to obligations of others, whether or not reflected on the balance sheet of the Person in question, including any obligation to furnish funds, directly or indirectly (whether by virtue of partnership arrangements, by agreement to keep-well, or otherwise), through the purchase of goods, supplies, or services, or by way of stock purchase, capital contribution, advance, or loan, or to enter into a contract for any of the foregoing, for the purpose of payment of obligations of any other

Person.

“Hazardous Materials” shall mean any substance (a) the presence of which requires notification, removal, or remediation under any Environmental Law; (b) that is or becomes defined as a “hazardous waste,” “hazardous material,” or “hazardous substance” under any present or future Environmental Law, or amendments thereto, including, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act (42 U.S.C. Section 9601, et seq.) and any applicable local statutes and the regulations promulgated thereunder; (c) that is toxic, explosive, corrosive, flammable, infectious, radioactive, carcinogenic, or otherwise hazardous and that is or becomes regulated pursuant to any Environmental Law; or (d) without limitation, that contains gasoline, diesel fuel, or other petroleum products, asbestos, or polychlorinated biphenyls.

“Indebtedness” shall mean, with respect to the Person in question, (a) all obligations of such Person for borrowed money or other extensions of credit, whether secured or unsecured, absolute or contingent, including, without limitation, unmatured reimbursement obligations with respect to letters of credit, and all obligations representing the deferred purchase price of property, (b) all obligations evidenced by bonds, notes, debentures, or other similar instruments, (c) all obligations secured by any Lien on property owned or acquired by the Person, (d) that portion of all obligations arising under leases that is required to be capitalized on the balance sheet of the Person, (e) all Guaranties executed by such Person, and (f) all other obligations that, in accordance with GAAP, should be included as a liability in the balance sheet of the Person.

“Indemnified Taxes” means any Taxes (other than Excluded Taxes) imposed on a Purchaser with respect to a payment under the Purchase Documents.

“Insolvency Proceeding” shall mean (a) any case, action or proceeding before any court or other Governmental Authority relating to bankruptcy, reorganization, insolvency, liquidation, receivership, dissolution, winding-up or relief of debtors, or (b) any general assignment for the benefit of creditors, composition, marshaling of assets for creditors, or other, similar arrangement in respect of its creditors generally or any substantial portion of its creditors; in each case in clauses (a) and (b) above, undertaken under U.S. Federal, state or foreign law, including the Bankruptcy Code.

“Inventory” shall mean means all inventory (as defined in RCW 62A.9A-102(a)(48), or any successor statute) of the Issuers.

“Investment” shall mean the purchase or acquisition of any share of Capital Stock, partnership interest, limited liability company interest, evidence of indebtedness, or other equity security of any other Person (including any Subsidiary or Affiliate), any loan, advance, or extension of credit (excluding Accounts arising in the ordinary course of business) to, or contribution to the capital of, any other Person (including any Subsidiary or Affiliate), any securities or commodities futures contracts held, any other investment in any other Person (including any Subsidiary or Affiliate), and the making of any commitment or acquisition of any option to make an Investment.

“Issuers” shall mean Nautilus initially and thereafter shall include any Subsidiary of Nautilus that becomes a co-issuer hereunder pursuant to Section 7.1(i).

“IRS” shall mean the Internal Revenue Service of the United States and any successor thereto.

“Lien” shall mean any mortgage, trust deed, pledge, charge, hypothecation, assignment, deposit arrangement, security interest, attachment, garnishment, execution, encumbrance (including, but not limited to, easements, rights of way, and the like), lien (statutory or other), security agreement, transfer intended as security (including, without limitation, any conditional sale or other title retention agreement, the interest of a lessor under a Capital Lease, or any financing lease having substantially the same economic effect as any of the foregoing), or other voluntary or involuntary lien or charge upon (or affecting the revenues of) any real property or personal property.

“Margin Stock” shall mean “margin stock” as such term is defined in Regulation T, U or X of the Federal Reserve Board.

“Material Adverse Effect” shall mean: (a) a material adverse effect on the business, assets, operations, or financial condition of any Issuer, (b) a material impairment of the ability of any Issuer to pay or perform its obligations under the Purchase Documents in accordance with the terms thereof or (c) a material impairment of

Purchasers' rights and remedies under the Purchase Documents.

" Non-U.S. Purchaser " means each Purchaser that is not a United States person as defined in Section 7701(a)(30) of the Code.

" Notes " shall have the meaning assigned to such term in Section 2.1 hereof.

" Obligations " shall mean all obligations under the Notes, and other Indebtedness, advances, debts, liabilities, obligations, covenants and duties owing by Nautilus or any Subsidiary of Nautilus that becomes a co-issuer pursuant to Section 7.1(i) hereunder to the Purchasers, or any other Person required to be indemnified, that arises under any Purchase Document, whether or not for the payment of money, whether arising by reason of an extension of credit, loan, guaranty, indemnification or in any other manner, whether direct or indirect (including those acquired by assignment), absolute or contingent, due or to become due, now existing or hereafter arising and however acquired.

" Other Taxes " shall have the meaning assigned to such term in Section 3.6 hereof.

" Patriot Act " shall mean the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, P.L. 107-56, as amended.

" Permitted Liens " shall have the meaning assigned to such term in Section 7.2(a) hereof.

" Person " shall mean an individual, sole proprietorship, partnership, corporation, limited liability company, business trust, joint stock company, trust, unincorporated association, joint venture, Governmental Authority, or other entity of whatever nature.

" Purchase Documents " shall mean this Agreement, the Notes and all other agreements, instruments and documents delivered in connection herewith or therewith, as any or all of the foregoing may be supplemented or amended from time to time.

" Purchaser " shall have the meaning assigned to such term in the introductory paragraph hereto and in Section 6.2 hereof and includes any Person that becomes a Purchaser by way of assignment, transfer or otherwise. With respect to any right or action to be taken by Purchasers under this Agreement, the word "Purchasers" shall mean all Purchasers, unless such word is included within the term "Requisite Purchasers", in which case the meaning of that term shall apply.

" Requisite Purchasers " shall mean, at any time, Purchasers owning an aggregate unpaid principal amount of greater than 50% of the aggregate Accreted Value of all the Notes outstanding at such time.

" Restricted Payments " means any dividend, distribution, or other similar payment (whether in cash or property) by the Issuers, and any purchase, redemption, retirement, or other acquisition for value of any capital stock or other ownership interests of the Issuers, whether now or hereafter outstanding, or of any options, warrants, or similar rights to purchase such capital stock or other ownership interests, or any security convertible into or exchangeable for such capital stock or other ownership interests.

" SEC " shall mean the U.S. Securities and Exchange Commission.

" Securities Act " shall mean the Securities Act of 1933, as amended.

" Senior Credit Agreement " shall mean that certain Credit Agreement, by and between Nautilus and the Senior Lender, dated March 8, 2010, as such may be amended or modified from time to time in compliance with the provisions of the Subordination Agreement, and any agreement evidencing a successive refunding or refinancing of the Indebtedness incurred thereunder, in each case subject to the terms and conditions of the Subordination Agreement.

" Senior Credit Documents " shall mean the Senior Credit Agreement and all other documents, agreements and instruments evidencing or pertaining to all or any portion of the Indebtedness incurred thereunder (including, without limitation, all "Loan Documents" as defined in the Senior Credit Agreement), including amendments, modifications, renewals and extensions thereof and all agreements or instruments evidencing successive refundings or refinancings of such Indebtedness, in each case subject to the terms and conditions of the Subordination Agreement.

&l dquo: Senior Lender ” shall collectively mean the lender and letter of credit issuer from time to time party to the Senior Credit Agreement or to any agreement evidencing a successive refunding or refinancing of the Indebtedness incurred thereunder, in each case subject to the terms and conditions of the Subordination Agreement.

“ Sherborne ” shall mean Sherborne Investors GP, LLC and its Affiliates.

“ Solvent ” shall mean, with respect to any Person on a particular date, that on such date (a) the fair value of the property of such Person, taken as a going concern, is greater than the total amount of liabilities, including contingent liabilities, of such Person; (b) the present fair salable value of the assets of such Person, taken as a going concern, is not less than the amount that will be required to pay the probable liability of such Person on its debts as they become absolute and matured; (c) such Person does not intend to, and does not believe that it will, incur debts or liabilities beyond such Person's ability to pay as such debts and liabilities mature; and (d) such Person is not engaged in a business or transaction, and is not about to engage in a business or transaction, for which such Person's property would constitute an unreasonably small capital. The amount of contingent liabilities (such as litigation, guaranties and pension plan liabilities) at any time shall be computed as the amount that, in light of all facts and circumstances existing at the time, represents the amount that can reasonably be expected to become an actual or matured liability.

“ Subordination Agreement ” shall have the meaning assigned to such term in Section 4.1(c) hereof.

“ Subsidiary ” shall mean any corporation, association, limited liability company, joint stock company, business trust, or other similar organization of which 50 percent or more of the ordinary voting power for the election of a majority of the members of the board of directors or other governing body of such entity is held or controlled by any Issuer; or any other such organization the management of which is directly or indirectly controlled by such Issuer through the exercise of voting power or otherwise; or any joint venture or partnership in which such Issuer has a 50 percent or greater ownership interest.

“ Taxes ” shall mean any present or future tax, assessment, duty, levy, impost, fee, deduction or withholding or other charge now or hereafter imposed, levied, collected, withheld or assessed by any Governmental Authority on any property, revenue, income, or franchise of any Person, and any interest, additions to tax or penalty with respect to any of the foregoing.

“ U.S. Purchaser ” means each Purchaser that is a United States person as defined in Section 7701(a)(30) of the Code.

“ United States ” and “ U.S. ” each shall mean the United States of America.

“ Voting Stock ” means Capital Stock issued by a corporation, or equivalent interests in any other Person, the holders of which are ordinarily, in the absence of contingencies, entitled to vote for the election of directors (or persons performing similar functions) of such Person, even though the right to so vote has been suspended by the happening of a contingency.

1.2 Accounting Principles .

(a) All accounting terms not specifically or completely defined herein shall be construed in conformity with, and all financial data (including financial ratios and other financial calculations) required to be submitted pursuant to this Agreement shall be prepared in conformity with, GAAP applied on a consistent basis, as in effect from time to time.

(b) If at any time any change in GAAP would affect the computation of any financial ratio or requirement set forth in any Purchase Document or any Senior Credit Document, and the Issuers and the Senior Lender amend such ratio or requirement in the Senior Credit Documents to preserve the original intent thereof in light of such change in GAAP, the Issuers and the Purchasers agree to promptly make conforming (after giving effect to the cushions in effect as of the Closing Date) amendments to the Purchase Documents.

1.3 Other Definitional Provisions: Construction . Whenever the context so requires, neuter gender includes the masculine and feminine, the singular number includes the plural and vice versa. The words “hereof”, “herein” and “hereunder” and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not in any particular provision of this Agreement, and references to section, article, annex, schedule, exhibit and like references are references to this Agreement unless otherwise specified. A Default or Event of Default shall

“continue” or be “continuing” until such Default or Event of Default has been cured or waived by (i) all Purchasers to the extent required by Section 9.3, (ii) the applicable Purchaser with respect to any Default or Event of Default under Section 8.1 hereof consisting of a failure to pay principal or interest on any Note held by such Purchaser and (iii) the Requisite Purchasers in all other instances. References in this Agreement to any Persons shall include such Persons' successors and permitted assigns.

ARTICLE 2

ISSUE AND SALE OF NOTES

2.1 Authorization and Issuance of the Notes . Nautilus has duly authorized the issuance and sale to Purchasers (or nominee of any Purchaser) of \$6,096,996.21 in aggregate principal amount at maturity of its Increasing Rate Senior Discount Notes Due December 31, 2012 (including any Notes issued in substitution therefor pursuant to Sections 6.3 and 6.4 hereof, the “Notes”), to be substantially in the form of the Note attached hereto as Exhibit A .

2.2 Sale and Purchase . Subject to the terms and conditions and in reliance upon the representations, warranties and agreements set forth herein, on the Closing Date Nautilus shall sell to Purchasers, and each Purchaser shall purchase from Nautilus, in an amount equal to its respective pro rata portion of the Notes as set forth on Annex A , the Notes in the aggregate principal amount at maturity set forth in Section 2.1 hereof for \$5,000,000 in the aggregate.

2.3 The Closing . Delivery of and payment for the Notes (the “ Closing ”) shall be made at the offices of Paul, Hastings, Janofsky & Walker LLP, New York, New York, commencing at 10:00 a.m., local time, on September 3, 2010, or at such place or on such other date as may be mutually agreeable to the Issuer and Purchasers. The date and time of the Closing as finally determined pursuant to this Section 2.3 are referred to herein as the “ Closing Date .” Delivery of the Notes shall be made to Purchasers against payment of the purchase price therefor and any other amounts payable pursuant to Section 4.1(e) hereof, by wire transfer of immediately available funds in the manner agreed to by the Issuer and Purchasers. The Notes shall be issued in such name or names and in such permitted denomination or denominations as set forth in Annex A .

ARTICLE 3

REPAYMENT OF THE NOTES

3.1 Accretion Rates and Interest Payments .

(a) Interest will accrete on the outstanding Accreted Value of the Notes at a rate equal to (i) 2.5% per annum from the Closing Date through February 28, 2011; (ii) 6.0% per annum from March 1, 2011 through August 31, 2011; (iii) 9.5% per annum from September 1, 2011 through February 29, 2012; (iv) 13.0% per annum from March 1, 2012 through August 31, 2012; and (v) 14.5% per annum thereafter, as such applicable rate may be increased in accordance with Section 8.2(c) . Accreted interest shall be automatically capitalized and added to the Accreted Value of the Notes on February 28, 2011, August 31, 2011, February 29, 2012 and August 31, 2012 and in each case shall thereafter accrue interest in accordance with the terms of this Agreement. Interest on the Notes will be computed on the basis of a year of 360 days, composed of 12, 30-day months, and the actual number of days elapsed.

3.2 Repayment of the Notes . The Issuers covenant and agree to repay Purchasers the unpaid principal balance of the Notes in full, together with all accreted and unpaid interest, fees and other amounts due hereunder, on December 31, 2012; provided , however , that such scheduled maturity date shall be automatically extended (without the consent of, or any action required by the Issuers or the Purchasers) by a number of days that the maturity date of the Senior Credit Agreement is extended; provided , further , that such scheduled maturity date may not be extended by more than 180 days without the consent of each Purchaser.

3.3 Optional Redemption of Notes . Subject to the terms of this Section 3.3 , on or after the date hereof, the Issuers may ratably prepay the Purchasers the outstanding principal amount of the Notes in whole or in part in multiples of \$100,000, or such lesser amount as is then outstanding, at any time at a price equal to the Accreted Value of the Notes as of the Specified Date of such repayment. Unless the Issuers default in the payment of the redemption price, interest will cease to accrete on the Notes or portions thereof called for redemption on the applicable redemption date. Upon surrender of a Note that is redeemed in part, the Issuers will issue, if requested by the Purchasers, at the Issuers' expense, a new Note equal in principal amount at maturity to the unredeemed portion of

the Note surrendered.

3.4 Notice of Optional Redemption . If the Issuers shall elect to redeem any Notes pursuant to Section 3.3 hereof, the Issuers shall give notice of such prepayment to Purchasers and each holder of the Notes to be prepaid not less than ten (10) days prior to the date fixed for redemption, specifying (a) the date on which such redemption is to be made, (b) the principal amount at maturity of such Notes to be redeemed on such date, and (c) the Accreted Value of the Notes to the date set for redemption. Such notice shall be accompanied by a certificate of the president or the chief financial officer of Nautilus that such redemption is being made in compliance with Section 3.3 hereof. Each redemption under this Section 3.4 shall consist of all amounts specified in such notice.

3.5 Home Office Payment . The Issuers will pay all sums becoming due on any Note for principal and interest to Purchasers, pro rata in accordance with the respective percentages of the Notes set forth on Annex A , by the method and at the address specified for such purpose in Annex A , or by such other method or at such other address as Purchasers shall have from time to time specified to the Issuers in writing for such purpose, without the presentation or surrender of such Note or the making of any notation thereon, except that promptly after payment or prepayment in full of any Note, each holder of a Note shall surrender such Note for cancellation to the Issuers at their respective principal executive offices.

3.6 Taxes .

(a) Any and all payments by the Issuers hereunder or under the Notes or other Purchase Documents that are made to or for the benefit of the Purchasers shall be made free and clear of and without deduction for any and all present or future Indemnified Taxes.

(b) If any Indemnified Taxes shall be required by law to be deducted from or in respect of any amount payable under any Purchase Document to any Purchaser (i) such amount shall be increased as necessary to ensure that, after all required deductions for Indemnified Taxes are made (including deductions applicable to any increases to any amount under this Section 3.6), such Purchaser receives the amount it would have received had no such deductions been made, (ii) the Issuers shall make such deductions, (iii) the Issuers shall timely pay the full amount deducted to the relevant taxing authority or other authority in accordance with applicable requirements of law and (iv) within 30 days after such payment is made, the Issuers shall deliver to the relevant Purchaser an original or certified copy of a receipt evidencing such payment.

(c) In addition, each Issuer agrees to pay any present or future stamp, documentary, excise, property, court, intangible, recording, filing or similar Tax, charges or similar levies imposed by any applicable requirement of law or Governmental Authority and all liabilities with respect thereto (including by reason of any delay in payment thereof), in each case arising from the execution, delivery, performance, enforcement, or perfection of a security interest under, or registration of, or otherwise with respect to, the Purchase Documents or any transaction contemplated therein (collectively, but excluding Excluded Taxes, the “ Other Taxes ”). Within 30 days after the date of any payment of Indemnified Taxes or Other Taxes by the Issuer, the Issuer shall furnish to the relevant Purchaser the original or a certified copy of a receipt evidencing payment thereof.

(d) The Issuers shall reimburse and indemnify, within 30 days after receipt of demand therefor, each Purchaser for all Indemnified Taxes and Other Taxes (including any Indemnified Taxes and Other Taxes imposed by any jurisdiction on amounts payable under this Section 3.6) paid by such Purchaser and any liabilities arising therefrom or with respect thereto, whether or not such Indemnified Taxes or Other Taxes were correctly or legally asserted; provided, that the Issuers shall not be required to compensate any Purchaser pursuant to this Section 3.6(d) for penalties, interest or other additions with respect to any Tax paid more than 180 days prior to the date that such Purchaser notifies the Issuers, in writing, of the Tax, and of such Purchaser's intention to claim compensation therefor. Payment of this indemnification shall be made within 30 days from the date the Purchasers provide the Issuers with a certificate setting forth in reasonable detail the calculation of the amount and type of such Taxes. Any such certificates submitted by the Purchasers in good faith to the Issuers shall, absent manifest error, be final, conclusive, and binding on all parties.

(e) Any Purchaser claiming any additional amounts payable pursuant to this Section 3.6 shall use its commercially reasonable efforts (consistent with its internal policies and requirements of law) to change the jurisdiction of its lending office if such a change would reduce any such additional amounts and would not, in the sole determination of such Purchaser, be otherwise disadvantageous to such Purchaser.

(f)

(i) Each Non-U.S. Purchaser that is entitled to an exemption from, or reduction of, United States withholding tax shall (y) on or prior to the date such Non-U.S. Purchaser becomes a “Non-U.S. Purchaser” hereunder and (z) from time to time if requested by the Issuers, provide the Issuers with two completed originals of each of the following, as applicable: (A) Forms W-8ECI (claiming exemption from U.S. withholding tax because the income is effectively connected with a U.S. trade or business), W-8BEN (claiming exemption from, or a reduction of, U.S. withholding tax under an income tax treaty)

and/or W-8IMY or any successor forms, (B) in the case of a Non-U.S. Purchaser claiming exemption under Sections 871(h) or 881(c) of the Code, Form W-8BEN (claiming exemption from U.S. withholding tax under the portfolio interest exemption) or any successor form and a certificate in form and substance acceptable to the Issuers that such Non-U.S. Purchaser is not (1) a “bank” within the meaning of Section 881(c)(3)(A) of the Code, (2) a “10 percent shareholder” of the Issuers within the meaning of Section 881(c)(3)(B) of the Code or (3) a “controlled foreign corporation” described in Section 881(c)(3)(C) of the Code or (C) any other applicable document prescribed by the IRS certifying as to the entitlement of such Non-U.S. Purchaser to such exemption, or reduced rate, from United States withholding tax with respect to all payments to be made to such Non-U.S. Purchaser under the Purchase Documents. Unless the Issuers have received forms or other documents satisfactory to them indicating that payments under the Purchase Documents to or for a Non-U.S. Purchaser are not subject to United States withholding tax or are subject to such tax at a rate reduced by an applicable tax treaty, the Issuers shall withhold amounts required to be withheld by applicable requirements of law from such payments at the applicable statutory rate. Notwithstanding any other provision of this paragraph, a Non-U.S. Purchaser shall not be required to deliver any form pursuant to this paragraph that such Non-U.S. Purchaser is not legally able to deliver.

(ii) Each U.S. Purchaser shall (y) on or prior to the date such U.S. Purchaser becomes a “U.S. Purchaser” hereunder and (z) from time to time if requested by the Issuer, provide the Issuer with two completed originals of Form W-9 (certifying that such U.S. Purchaser is entitled to an exemption from U.S. backup withholding tax) or any successor form. Notwithstanding any other provision of this paragraph, a U.S. Purchaser shall not be required to deliver any form pursuant to this paragraph that such U.S. Purchaser is not legally able to deliver.

(iii) In addition, if a payment made to a Purchaser with respect to the Purchase Documents would be subject to U.S. federal withholding Tax imposed by FATCA if such Purchaser fails to comply with the applicable reporting requirements of FATCA (including those contained in section 1471(b) or 1472(b) of the Code, as applicable), such Purchaser shall deliver to the Issuers any documentation required by law or reasonably requested by the Issuers sufficient for the Issuers to comply with their obligations under FATCA and to determine that such Purchaser has complied with such applicable reporting requirements.

(g) If any Purchaser determines in its sole discretion that it has received a refund of any Indemnified Taxes or Other Taxes as to which it has been indemnified by the Issuers or with respect to which the Issuers have paid additional amounts pursuant to this Section 3.6, it shall pay to the Issuers an amount equal to such refund (but only to the extent of indemnity payments made, or additional amounts paid, by the Issuers under this Section 3.6 with respect to the Indemnified Taxes or Other Taxes giving rise to such refund), net of all out-of-pocket expenses of such Purchaser, and without interest (other than any interest paid by the relevant Governmental Authority with respect to such refund), provided that the Issuers, upon the request of such Purchaser, agrees to repay the amount paid over to the Issuers (plus any penalties, interest or other charges imposed by the relevant Governmental Authority) to the Purchaser in the event such Purchaser is required to repay such refund to such Governmental Authority. This paragraph shall not be construed to require any Purchaser to make available its tax returns (or any other information relating to its taxes which it deems confidential) to the Issuers or to any other Person.

3.7 Maximum Lawful Rate. This Agreement, the Notes and the other Purchase Documents are hereby limited by this Section 3.7. In no event, whether by reason of acceleration of the maturity of the amounts due hereunder or otherwise, shall interest and fees contracted for, charged, received, paid or agreed to be paid to Purchasers exceed the maximum amount permissible under such applicable law. If, from any circumstance whatsoever, interest and fees would otherwise be payable to Purchasers in excess of the maximum amount permissible under such applicable law, the interest and fees shall be reduced to the maximum amount permitted under applicable law. If from any circumstance, Purchasers shall have received anything of value deemed interest by applicable law in excess of the

maximum lawful amount, an amount equal to any excess of interest shall be applied to the reduction of the principal amount of the Notes, in such manner as may be determined by Purchasers, and not to the payment of fees or interest, or if such excessive interest exceeds the unpaid balance of the principal amount of the Notes, such excess shall be refunded to the Issuers.

3.8 Certain Waivers . The Issuers unconditionally waive (a) any rights to presentment, demand, protest or (except as expressly required hereby) notice of any kind, and (b) any rights of rescission, setoff, counterclaim or defense to payment under the Notes or otherwise that the Issuers may have or claim against any Purchaser or any prior Purchaser.

3.9 Joint and Several Liability of the Issuers . To the extent that any Subsidiary of Nautilus becomes a co-issuer hereunder pursuant to Section 7.1(i) :

(a) Each Issuer is accepting joint and several liability hereunder and under the other Purchase Documents in consideration of the financial accommodations to be provided by the Purchasers under this Agreement, for the mutual benefit, directly and indirectly, of each Issuer and in consideration of the undertakings of the other Issuers to accept joint and several liability for the Obligations.

(b) Each Issuer, jointly and severally, hereby irrevocably and unconditionally accepts, not merely as a surety but also as a co-debtor, joint and several liability with the other Issuers, with respect to the payment and performance of all of the Obligations (including, without limitation, any Obligations arising under this Section 3.9), it being the intention of the parties hereto that all the Obligations shall be the joint and several obligations of each Issuer without preferences or distinction among them.

(c) If and to the extent that any Issuer shall fail to make payment with respect to any of the Obligations as and when due or to perform any of the Obligations in accordance with the terms thereof, then in each such event the other Issuers will, without duplication, make such payment with respect to, or perform, such Obligation.

(d) The Obligations of each Issuer under the provisions of this Section 3.9 constitute the absolute and unconditional, full recourse Obligations of each Issuer enforceable against each Issuer to the full extent of its properties and assets.

(e) Except as otherwise expressly provided in this Agreement, each Issuer hereby waives notice of acceptance of its joint and several liability, notice of the occurrence of any Default or Event of Default or of any demand for any payment under this Agreement, notice of any action at any time taken or omitted by the Purchasers under or in respect of any of the Obligations, any requirement of diligence or to mitigate damages and, generally, to the extent permitted by applicable law, all demands, notices and other formalities of every kind in connection with this Agreement (except as otherwise provided in this Agreement). Each Issuer hereby assents to, and waives notice of, any extension or postponement of the time for the payment of any of the Obligations, the acceptance of any payment of any of the Obligations, the acceptance of any partial payment thereon, any waiver, consent or other action or acquiescence by the Purchasers at any time or times in respect of any default by any Issuer in the performance or satisfaction of any term, covenant, condition or provision of this Agreement, any and all other indulgences whatsoever by the Purchasers in respect of any of the Obligations, and the taking, addition, substitution or release, in whole or in part, at any time or times, of any security for any of the Obligations or the addition, substitution or release, in whole or in part, of any Issuer. Without limiting the generality of the foregoing, each Issuer assents to any other action or delay in acting or failure to act on the part of the Purchasers with respect to the failure by any Issuer to comply with any of its respective Obligations, including, without limitation, any failure strictly or diligently to assert any right or to pursue any remedy or to comply fully with applicable laws or regulations thereunder, which might, but for the provisions of this Section 3.9 afford grounds for terminating, discharging or relieving any Issuer, in whole or in part, from any of its Obligations under this Section 3.9 , it being the intention of each Issuer that, so long as any of the Obligations hereunder remain unsatisfied, the Obligations of each Issuer under this Section 3.9 shall not be discharged except by performance and then only to the extent of such performance. The Obligations of each Issuer under this Section 3.9 shall not be diminished or rendered unenforceable by any winding up, reorganization, arrangement, liquidation, reconstruction or similar proceeding with respect to any Issuer or Purchaser.

(f) Each Issuer represents and warrants to Purchasers that such Issuer is currently informed of the financial condition of the other Issuers and of all other circumstances which a diligent inquiry would reveal and which bear upon the risk of nonpayment of the Obligations. Each Issuer further represents and warrants to Purchasers that such Issuer has read and understands the terms and conditions of the Purchase Documents. Each Issuer hereby covenants

that such Issuer will continue to keep informed of such Issuer's financial condition, the financial condition of other guarantors and of all other circumstances which bear upon the risk of nonpayment or nonperformance of the Obligations.

(g) The provisions of this Section 3.9 are made for the benefit of the Purchasers and their successors, nominees and assigns, and may be enforced by it or them from time to time against any or all Issuers as often as occasion therefor may arise and without requirement on the part of any such Purchaser, successor or assign first to marshal any of its or their claims or to exercise any of its or their rights against any Issuer or to exhaust any remedies available to it or them against any Issuer or to resort to any other source or means of obtaining payment of any of the Obligations hereunder or to elect any other remedy. The provisions of this Section 3.9 shall remain in effect until all of the Obligations (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted) shall have been paid in full or otherwise fully satisfied. If at any time, any payment, or any part thereof, made in respect of any of the Obligations, is rescinded or must otherwise be restored or returned by any Purchaser upon the insolvency, bankruptcy or reorganization of any Issuer, or otherwise, the provisions of this Section 3.9 will forthwith be reinstated in effect, as though such payment had not been made.

(h) Each Issuer hereby agrees that it will not enforce any of its rights of contribution or subrogation against any other Issuer with respect to any liability incurred by it hereunder or under any of the other Purchase Documents, any payments made by it to Purchasers with respect to any of the Obligations until such time as all of the Obligations (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted) have been paid in full in cash. Any claim which any Issuer may have against any other Issuer with respect to any payments to any Purchaser hereunder or under any other Purchase Documents are hereby expressly made subordinate and junior in right of payment, without limitation as to any increases in the Obligations arising hereunder or thereunder, to the prior payment in full in cash of the Obligations (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted) and, in the event of any insolvency, bankruptcy, receivership, liquidation, reorganization or other similar proceeding under the laws of any jurisdiction relating to any Issuer, its debts or its assets, whether voluntary or involuntary, all such Obligations (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted) shall be paid in full in cash before any payment or distribution of any character, whether in cash, securities or other property, shall be made to any other Issuer therefor.

ARTICLE 4

CONDITIONS

4.1 Conditions to Purchase of Notes . The obligation of Purchasers to purchase and pay for the Notes is subject to the satisfaction or waiver, prior to or at the Closing, of the following conditions:

(a) Representations and Warranties True . The representations and warranties contained in Article 5 hereof shall be true and correct in all material respects at and as of the Closing Date as though then made, except (i) to the extent of changes caused by the transactions expressly contemplated herein and (ii) for representations and warranties that are by their terms already qualified by materiality or Material Adverse Effect, which representations and warranties described in this clause (ii) shall be true and correct in all respects.

(b) Material Adverse Effect . There will have been no Material Adverse Effect since June 30, 2010.

(c) Subordination Agreement . Purchasers, the Senior Lender and the Issuers shall have executed a subordination and intercreditor agreement (the “Subordination Agreement”) on terms reasonably satisfactory to Purchasers.

(d) Closing Documents . The Issuers shall have delivered or caused to be delivered to Purchasers all of the following documents in form and substance reasonably satisfactory to Purchasers:

(i) one or more Notes (as designated by Purchasers pursuant to Section 2.1 and Annex A hereof) in aggregate original principal amounts at maturity as set forth herein, duly completed and executed by the Issuers;

(ii) a certificate of good standing dated not more than fourteen (14) days prior to the Closing Date for each Issuer, issued by its jurisdiction of organization;

(iii) a copy of the certificate of incorporation of each Issuer, certified by the appropriate governmental official of the jurisdiction of its organization as of a date not more than fourteen (14) days prior to the Closing Date;

(iv) a copy of the By-laws of each Issuer, certified as of the Closing Date by the secretary or assistant secretary of such Issuer;

(v) certificates of the secretary or assistant secretary of each Issuer, certifying as to the names and true signatures of the officers or other authorized person of such Issuer authorized to sign the Purchase Documents to be delivered by it hereunder;

(vi) copies of the resolutions duly adopted by the board of directors of each Issuer authorizing the execution, delivery and performance by it of the Purchase Documents to which it is a party, and the consummation of the transactions contemplated hereby evidenced thereby, respectively, certified as of the Closing Date by its secretary or assistant secretary; and

(vii) an opinion of Kirkland & Ellis LLP, counsel to the Issuers, in form and substance reasonably satisfactory to Purchasers.

(e) Purchasers' Fees and Expenses . On the Closing Date, the Issuers shall have paid all fees and expenses (to the extent invoiced prior to the Closing Date) of Purchasers payable by the Issuers pursuant to Section 9.4 hereof.

(f) Legal Investment . On the Closing Date, Purchasers' purchases of the Notes shall not be prohibited by any applicable law, rule or regulation of any Governmental Authority (including, without limitation, Regulations T, U or X of the Federal Reserve Board) as a result of the promulgation or enactment thereof or any changes therein, or change in the interpretation thereof by any Governmental Authority.

Any condition specified in this Section 4.1 may be waived by Purchasers; provided , however , that no such waiver will be effective against any Purchaser unless it is set forth in writing, executed by such Purchaser.

ARTICLE 5

REPRESENTATIONS AND WARRANTIES OF THE ISSUERS

The Issuers represents and warrants to the Purchasers as follows:

5.1 Existence and Power of Issuers . Each Issuer is a corporation duly organized and existing under the laws of the state of its incorporation and is qualified to do business in each jurisdiction where the failure to be so qualified could be reasonably likely to result in a Material Adverse Effect. Each Issuer has full power, authority, and legal right to carry its businesses as presently conducted, to own and operate its properties and assets, and to execute, deliver, and perform this Agreement and the other Purchase Documents.

5.2 Authorization by Issuers . The execution, delivery, and performance by each Issuer of this Agreement, the Notes, and the other Purchase Documents, have been duly authorized by all necessary corporate action of each Issuer, does not require shareholder approval, or the approval or consent of any trustee or the holders of any Indebtedness of any Issuer, does not contravene any law, regulation, rule, or order binding on any Issuer, or any of the Issuers' organizational documents, and do not contravene the provisions of or constitute a default under any indenture, mortgage, material contract, or other material agreement or instrument to which any Issuer is a party, or by which any Issuer (or any of its properties) may be bound or affected.

5.3 Governmental Approvals . No Government Approval or filing or registration with any Governmental Authority is required for the making and performance by each Issuer of this Agreement or any Purchase Document, or in connection with any of the transactions contemplated hereby, except those that have been obtained or made and are in full force and effect. Each Issuer has obtained all Governmental Approvals that are necessary or required in connection with the conduct of such Issuer's business, except any Governmental Approvals the failure to obtain which could not be reasonably likely to result in a Material Adverse Effect.

5.4 Binding Obligations . This Agreement, the Notes, and the other Purchase Documents have been duly executed and delivered by each Issuer and constitute the legal, valid, and binding obligations of each Issuer. This Agreement, the Notes, and the other Purchase Documents are enforceable against each Issuer and its property in

accordance with their respective terms, except as limited by bankruptcy, insolvency, reorganization, moratorium, or other similar laws affecting the enforcement of creditors' rights generally, and except as the remedy of specific performance, or the remedy of injunctive relief, is subject to the discretion of the court before which any proceeding therefor may be brought.

5.5 Litigation . Except as specifically disclosed in Schedule 5.5 , there are no actions, proceedings, investigations, or claims against or affecting any Issuer now pending before any court, arbitrator, or Governmental Authority, which individually or in the aggregate, could be reasonably likely to result in a Material Adverse Effect.

5.6 No Default . No Default or Event of Default exists or would result from the issuance of the Notes. None of the Issuers nor any of their respective Subsidiaries is in breach of or default under any agreement to which it is a party, or that is binding on it (or any of its respective assets), except to the extent any such breach or default could not be reasonably likely to result in a Material Adverse Effect.

5.7 Margin Regulations . The Issuers are not engaged principally or as one of the Issuers' important activities in the business of extending credit for the purpose of purchasing or carrying any margin stock (within the meaning of Federal Reserve Regulation U), and no part of the proceeds of any Revolving Loan will be used to purchase or carry any such margin stock, or to extend credit to others for the purpose of purchasing or carrying any such margin stock, or for any other purpose that violates the applicable provisions of any Federal Reserve Regulation. If requested to do so by the Purchasers, the Issuers will furnish to the Purchasers a statement conforming with the requirements of Regulation U.

5.8 Compliance With Laws . The Issuers are in compliance in all respects with all laws, regulations, rules, and orders of Governmental Authorities applicable to the Issuers, or to the Issuers' operations or property (including, but not limited to, Environmental Laws, Consumer Protection Laws and ERISA), except any thereof whose validity is being contested in good faith by appropriate proceedings upon stay of execution of the enforcement thereof and except to the extent any non-compliance could not be reasonably likely to result in a Material Adverse Effect.

5.9 Title to Properties . Each Issuer has good and marketable title to all of its material properties and assets. The properties and assets of each Issuer is subject to no Liens, other than Permitted Liens.

5.10 Taxes . Each Issuer has timely filed all federal and state and all other material tax returns and reports required of such Issuer and has paid all material Taxes that are due and payable (except to the extent such Taxes are being properly contested in good faith by appropriate legal proceedings). The charges and accruals on the books of each Issuer in respect of Taxes for all fiscal periods to date are accurate in all material respects. Taxes not yet due have been provided for as a reserve on the books of each Issuer to the extent required under GAAP. There are no claims or assessments against any Issuer by any Governmental Authority with respect to any Taxes, except any claims or assessments that could not be reasonably likely to result in a Material Adverse Effect.

5.11 Financial Condition .

(a) Each Issuer has delivered to Purchasers such Issuer's report on Form 10-K for the fiscal year ended December 31, 2009 and its Form 10-Q for fiscal quarter ending June 30, 2010 as filed with the SEC, and the financial statements contained in such reports present fairly in all material respects such Issuer's financial condition and results of operations for the periods covered thereby, and such financials have been prepared in accordance to GAAP.

(b) Since June 30, 2010, there has been no Material Adverse Effect.

5.12 Solvency . Both before and after giving effect to the issuance of the Notes, each Issuer is Solvent.

5.13 Labor Relations . There is (a) no unfair labor practice complaint pending against any Issuer or, to the best knowledge of the Issuers, threatened, before the National Labor Relations Board, and no grievance or arbitration proceeding arising out of or under any collective bargaining agreement is so pending against any Issuer or, to the best knowledge of the Issuers, threatened, and (b) no strike, labor dispute, slowdown, or stoppage pending against any Issuer or, to the best knowledge of the Issuers, threatened against any Issuer, except, in each case, to the extent such complaint, strike, labor dispute, slowdown or stoppage could not be reasonably likely to result in a Material Adverse Effect.

5.14 Intellectual Property; Licenses, Etc. . Each Issuer owns, licenses or otherwise possesses the right to use,

all material trademarks, service marks, trade names, copyrights, patents, patent rights, franchises, licenses and other intellectual property rights that are reasonably necessary for the operation of its businesses, without conflict with the rights of any other Person, except to the extent such conflict could not be reasonably likely to result in a Material Adverse Effect. To the knowledge of the Issuers, no slogan or other advertising device, product, process, method, substance, part or other material now employed, or now contemplated to be employed, by any Issuer infringes upon any rights held by any other Person in any material respect. No claim or litigation regarding any of the foregoing is pending or, to the knowledge of the Issuers, threatened.

5.15 Brokers' Fees . No Issuer has any obligation to any Person in respect of any finder's, broker's or investment banker's fee in connection with the transactions contemplated hereby, except for such fees payable to D.A. Davidson & Co. with respect to advice and analysis performed for the Board of Directors of Nautilus in connection with the issuance of the Notes to the Purchasers.

5.16 Full Disclosure . No information contained in this Agreement, any of the other Purchase Documents, any projections, financial statements or collateral reports or other written reports from time to time delivered hereunder or any written statement furnished by or on behalf of the Issuers to the Purchasers pursuant to the terms of this Agreement contains or will contain any untrue statement of a material fact or omits or will omit to state a material fact necessary to make the statements contained herein or therein not materially misleading in light of the circumstances under which they were made.

5.17 Similar Offerings . Nautilus has not and none of its affiliates, as such term is defined in Rule 501(b) under the Securities Act (other than Sherborne, as to which no representation or warranty is being made), has, directly or indirectly, solicited any offer to buy, sold or offered to sell or otherwise negotiated in respect of, or will solicit any offer to buy, sell or offer to sell or otherwise negotiate in respect of, in the United States or to any United States citizen or resident, any security which is or would be integrated with the sale of the Notes in a manner that would require the offered Notes to be registered under the Securities Act.

5.18 No General Solicitation . Nautilus has not and no person acting on its behalf (other than Sherborne, as to which no representation or warranty is being made) has engaged or will engage, in connection with the offering of the offered Notes, in any form of general solicitation or general advertising within the meaning of Rule 502(c) under the Securities Act.

5.19 Private Offering; Consents and Approvals . No consent, approval, order or authorization of, or registration, qualification, designation, declaration or filing with, any federal, state or local governmental authority on the part of the Issuers is required in connection with the offer, sale or issuance of the Notes or the consummation of any other transactions contemplated hereby, except for the compliance with applicable state securities laws, which compliance will have occurred

within the appropriate time periods therefor. Assuming that the representations of the Purchasers set forth in Section 6.2 are true and correct, the offer, sale and issuance of the Notes in conformity with the terms of this Agreement are exempt from the registration requirements of Section 5 of the Securities Act, and from the qualification requirements of each applicable state securities laws, and neither the Issuers, nor any authorized agent acting on their behalf will take any action hereafter that would cause the loss of such exemptions.

5.20 Absolute Reliance on the Representations and Warranties . All representations and warranties contained in this Agreement and any financial statements, instruments, certificates, schedules or other documents delivered in connection herewith shall survive the execution and delivery of this Agreement, regardless of any investigation made by Purchasers or on Purchasers' behalf.

ARTICLE 6

TRANSFER OF NOTES

6.1 Restricted Securities . Purchasers acknowledge that the Notes have not been registered under the Securities Act and may be resold only if registered pursuant to the provisions of the Securities Act or if an exemption from registration is available, and that the Issuers are not required to register the Notes.

6.2 Legends; Purchasers' Representations . Each of the Purchasers hereby represents and warrants to the Issuers that (a) it is an "accredited investor" within the meaning of Rule 501(a) under the Securities Act and is acquiring

the Notes for investment for its own account, with no present intention of dividing its participation with others or reselling or otherwise distributing the same in violation of the Securities Act or any applicable state securities laws and (b) such Purchaser is not purchasing Notes as a result of any advertisement, article, notice or other communication published in any newspaper, magazine or similar media or broadcast over television or radio, any seminar or meeting, or any solicitation by a person not previously known to such Purchaser in connection with investments in securities generally. The Issuers may place an appropriate legend on the Notes owned by Purchasers concerning the restrictions set forth in this Article 6. Upon the assignment or transfer by Purchasers or any of its successors or assignees of all or any part of the Notes, the term “Purchaser” as used herein shall thereafter mean, to the extent thereof, the then holder or holders of such Notes, or portion thereof. In connection with the issuance of the Notes to the Purchasers, each Purchaser makes the following representations and warranties to the Issuers as of the date of such issuance:

(a) Such Purchaser has such knowledge and experience in financial and business matters as to be capable of making an informed decision regarding an investment in the Notes and is capable of reviewing, understanding and making an independent judgment with respect to an investment in the Notes; and

(b) Such Purchaser acknowledges that it has been advised by the Issuers to consult such Purchaser's own legal, financial and tax advisors concerning this investment. Such Purchaser acknowledges that it has reviewed the risks and merits of an investment in the Notes with tax, legal and investment advisors to the extent deemed advisable by such Purchaser.

(c) Such Purchaser acknowledges that the face of each Note shall be endorsed with a legend substantially in the form set forth below:

“THIS NOTE HAS BEEN ISSUED WITH “ORIGINAL ISSUE DISCOUNT” (WITHIN THE MEANING OF SECTION 1273 OF THE INTERNAL REVENUE CODE OF 1986, AS AMENDED (THE “CODE”)). UPON WRITTEN REQUEST, THE ISSUER WILL PROMPTLY MAKE AVAILABLE TO ANY HOLDER OF THIS NOTE THE FOLLOWING INFORMATION: (1) THE ISSUE PRICE AND ISSUE DATE OF THE NOTE, (2) THE AMOUNT OF ORIGINAL ISSUE DISCOUNT ON THE NOTE AND (3) THE YIELD TO MATURITY OF THE NOTE. THE HOLDER OF THIS NOTE CAN OBTAIN THIS INFORMATION BY CONTACTING NAUTILUS, INC. AT 16400 S.E. NAUTILUS DRIVE, VANCOUVER, WA 98683, ATTN: ALEC ANDERSON.”

6.3 Transfer of Notes. (a) Subject to Sections 6.1 and 6.2 hereof, a holder of a Note (x) may transfer such Note or a portion thereof to any other Person, or (y) may exchange such Note for Notes of different denominations, by surrendering such Note to the Issuers duly endorsed for transfer or accompanied by a duly executed instrument of transfer naming the new holder (or the current holder if submitted for exchange only), together with written instructions for the issuance of one or more new Notes specifying the respective principal amounts of each new Note and the name of each new holder and each address therefor. The Issuers shall simultaneously deliver to such holder or its designee such new Notes, shall mark the surrendered Notes as canceled and shall provide notice of such transfer to Purchasers. In lieu of the foregoing procedures, but subject to Sections 6.1 and 6.2 hereof and to the provisions of Section 6.3(a)(x) above, a holder may assign a Note (in whole but not in part) to a new holder by sending written notice to the Issuers and Purchasers of such assignment specifying the new holder's name and address; in such case, the Issuers shall promptly acknowledge such assignment in writing to both the old and new holder. The Issuers shall not be required to recognize any subsequent holder of a Note unless and until the Issuers have received reasonable assurance that all applicable transfer taxes have been paid. No assignee or transferee of a Note shall be entitled to receive any greater payment under Section 3.7 hereof than the applicable Purchaser that assigned or transferred such Note to such assignee or transferee would have been entitled to receive under such Section.

(b) Notwithstanding anything to the contrary contained in this Agreement, the Notes are registered obligations and the right, title and interest of the Purchasers in and to such Notes, as the case may be, shall be transferable only in accordance with the terms hereof. This Section 6.3 shall be construed so that the Notes are at all times maintained in “registered form” within the meaning of Sections 163(f), 871(h)(2) and 881(c)(2) of the Code.

6.4 Replacement of Lost Notes. Upon receipt of evidence reasonably satisfactory to the Issuers of the mutilation, destruction, loss or theft of any Notes and the ownership thereof, the Issuers shall, upon the written request of the holder of such Notes, execute and deliver in replacement thereof new Notes in the same form, in the same original principal amount and dated the same date as the Notes so mutilated, destroyed, lost or stolen; and such Notes so mutilated, destroyed, lost or stolen shall then be deemed no longer outstanding hereunder. If the Notes being replaced

have been mutilated, they shall be surrendered to the Issuers; and if such replaced Notes have been destroyed, lost or stolen, such holder shall furnish the Issuers with an indemnity in writing to save it harmless in respect of such replaced Note.

6.5 No Other Representations Affected . Nothing contained in this Article 6 shall limit the full force or effect of any representation, agreement or warranty made herein or in connection herewith to Purchasers.

ARTICLE 7

COVENANTS

7.1 Affirmative Covenants . Each Issuer covenants and agrees that, so long as any Note or any other Obligation (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted) shall remain unpaid or unsatisfied:

(a) Financial Statements . Each Issuer shall deliver to each Purchaser in electronic form and in detail reasonably satisfactory to the Purchasers:

(i) within forty-five (45) days of the end of each calendar quarter, the unaudited balance sheet and statements of cash flow, income, and retained earnings of such Issuer for the immediately preceding quarter (and for the period from the start of such Issuer's then-current fiscal year through the last day of the immediately preceding quarter) on a consolidated and consolidating basis (it being agreed that the furnishing of such Issuer's report on Form 10-Q for such fiscal quarter as filed with the SEC will satisfy such requirement);

(ii) within one hundred twenty (120) days of each fiscal year end of such Issuer, a copy of an audited statement (on a consolidated and consolidating basis) of such Issuer's financial condition as of the end of the preceding fiscal year prepared by a certified public accounting firm reasonably acceptable to the Requisite Purchasers (it being agreed that the furnishing of such Issuer's annual report on Form 10-K for such fiscal year as filed with the SEC will satisfy such requirement); and

(iii) Other Information . All other statements, reports, and information as the Purchasers reasonably may request concerning the Notes, or the financial condition and business affairs of the Issuers, their respective Subsidiaries, and their Affiliates.

(b) Preservation of Existence, Etc. Except as otherwise permitted in this Agreement, each Issuer shall preserve and maintain its corporate existence, rights, franchises, and privileges in the jurisdiction of its organization and shall qualify and remain qualified as a foreign organization in each jurisdiction where the failure to do so could be reasonably likely to result in a Material Adverse Effect.

(c) Keeping of Books and Records . Each Issuer shall keep adequate records and books of account in which entries complete in all material respects will be made, in accordance with GAAP, reflecting all financial transactions of Issuer.

(d) Maintenance of Property . Each Issuer shall maintain and preserve its respective properties which are material to its business in good working order and condition, ordinary wear and tear and casualty (to the extent insured) excepted, and shall from time to time make all needed repairs, renewals, or replacements so that the efficiency of such properties shall be fully maintained and preserved.

(e) Insurance . Each Issuer shall keep in force upon all of its respective properties and operations policies of insurance carried with companies in such amounts and covering all such risks as shall be customary in the industry.

(f) Payment of Obligations; Notice of Default under Senior Credit Agreement . Each Issuer shall pay and discharge before the same shall become delinquent all material Indebtedness, Taxes, and other material obligations for which it is liable, or to which the income or property of such Issuer is subject, and all claims for labor, materials, or supplies that, if unpaid, might become by law a Lien upon assets of such Issuer, except such Indebtedness, Taxes, claims, and obligations that are being contested in good faith by appropriate proceedings; provided that a breach of the foregoing with respect to the Senior Loan Documents shall not be an Event of Default hereunder unless the Senior Lender has accelerated the obligations under the Senior Loan Documents as a result thereof. Nautilus agrees that it shall give the Purchasers prompt written notice of any "default" or "event of default" under or within the </div>

meaning of any of the Senior Loan Documents, in each case of which such Issuer has knowledge at the same time such notice is given to the Senior Lender or received by such Issuer from the Senior Lender.

(g) Compliance with Laws . Subject to the right to contest any laws, regulations, rules or orders of any Governmental Authority in good faith by appropriate legal proceedings, and provided that each Issuer establishes and maintains adequate reserves to the extent required by GAAP in relation to the matter being contested, each Issuer shall comply with all laws, regulations, rules, and orders of any Governmental Authority applicable to them, including, but not limited to, Environmental Laws, Consumer Protection Laws and ERISA, except where failure to so comply could not be reasonably likely to result in a Material Adverse Effect.

(h) Use of Proceeds . The Issuers shall use the proceeds of the Notes solely for working capital and other general corporate purposes.

(i) Further Assurances .

(i) Upon written demand by a Purchaser, the Issuers shall promptly execute and deliver all such instruments and perform all such other acts as such Purchaser may reasonably request to carry out the transactions contemplated by this Agreement or any other Purchase Document.

(ii) With respect to any Domestic Subsidiary created or acquired after the Closing Date by any Issuer, the Issuers shall promptly, and in any event on or prior to 20 days after such creation or acquisition (A) cause such Domestic Subsidiary to execute and deliver a joinder to this Agreement and the other Purchase Documents, in form and substance reasonably satisfactory to the Purchasers and (B) if reasonably requested by the Purchasers, deliver to the Purchasers legal opinions and secretary's certificates relating to the matters described above, which opinions and certificate s shall be in form and substance substantially similar to those delivered on the Closing Date.

7.2 Negative Covenants . Each Issuer covenants and agrees that, so long as any Note or other Obligation (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted) shall remain unpaid or unsatisfied:

(a) Limitation on Liens . The Issuers shall not create, incur, assume, or suffer to exist any Lien of any kind upon or with respect to any of its property or assets, or assign or otherwise convey any right to receive income, including the sale or discount of Accounts with or without recourse, except the following (" Permitted Liens "):

(i) Liens in favor of lenders under the Senior Credit Documents;

(ii) Liens existing as of the date of this Agreement and disclosed in Schedule 7.2(a) to this Agreement;

(iii) Liens for Taxes, assessments, or other governmental charges not delinquent or being contested in good faith and by appropriate proceedings and with respect to which proper reserves have been taken by Issuer; provided, however, that the Lien shall have no effect on the value of such assets and, provided further, that a stay of enforcement of any such Lien (other than such inchoate tax Liens) shall be in effect;

(iv) Landlords' and lessors' Liens in respect of rent not in default, or Liens in respect of pledges or deposits under workers' compensation, unemployment insurance, social security laws, or similar legislation (other than ERISA), or in connection with appeal and similar bonds incidental to litigation; mechanics', warehousemen's, laborers', and materialmen's and similar Liens, if the obligations secured by such Liens are not then delinquent;

(v) Easements, rights of way, restrictions, and other similar charges or Liens relating to real property and not interfering in a material way with the ordinary conduct of any Issuer's businesses;

(vi) Liens constituting a renewal, extension, or replacement of any Permitted Lien;

(vii) Purchase money Liens in connection with Indebtedness permitted under Section 7.2(c);

(viii) Deposits of cash with the owner or lessor of premises leased and operated by any Issuer in the ordinary course of business to secure the performance by any Issuer of its obligations under the terms of the lease for such premises;

(ix) Liens arising from precautionary Uniform Commercial Code filings regarding "true" operating leases or the consignment of goods to any Issuer;

(x) Liens arising by operation of law under Article 2 of the Uniform Commercial Code in favor of a reclaiming seller of goods or buyer of goods;

(xi) Normal and customary rights of setoff upon deposits in favor of depository institutions, and Liens of a collecting bank on payment items in the course of collection;

(xii) Licenses of intellectual property owned by any Issuer and granted to any person in the ordinary course of business and any restrictions or conditions on transfer, assignment or renewal customarily imposed in a license to use intellectual property;

(xiii) Judgments and other similar Liens arising in connection with court proceedings that do not constitute a Default or Event of Default;

(xiv) Pledges and deposits of cash of less than \$1,000,000 to secure obligations under appeal bonds or as otherwise required in connection with court proceedings (including, without limitation, surety bonds, security for costs of litigation where required by law and letters of credit) or any other instruments serving a similar purpose;

(xv) Liens in favor of an insurance company to secure Indebtedness permitted in Section 7.2(c) hereof to finance insurance premiums; and

(xvi) Liens in the nature of rights of set off in favor of contractual counterparties in the ordinary course of business.

(b) Liquidation, Merger, or Sale of Assets . No Issuer shall (i) liquidate, dissolve, or enter into any merger or consolidation in which such Issuer would not be the surviving entity, or (ii) sell, lease, or dispose of any material portion of the business or assets of such Issuer (except (A) sales of goods in the ordinary course of business; (B) sales or other dispositions of surplus or obsolete equipment in the ordinary course of business; (C) disposition of any property in connection with discontinuation of Business; (D) dispositions of Inventory that is obsolete, unmerchantable or otherwise unsalable in the ordinary course of business; (E) termination of any lease of real or personal property that is not necessary for the ordinary course of business of such Issuer, could not reasonably be expected to have a Material Adverse Effect and does not result from such Issuer's default thereunder; (F) licenses, sublicenses, leases or subleases granted to others not interfering in any material respect with the business of such Issuer and which could not reasonably be expected to have a Material Adverse Effect; (G) sales or dispositions of cash and cash equivalents in the ordinary course of business which are not reasonably likely to have a Material Adverse Effect; (H) abandonment of intellectual property of such Issuer that is immaterial, unnecessary or no longer used in the ordinary course of business, the abandonment of which could not reasonably be expected to have a Material Adverse Effect; (I) dispositions of Accounts not constituting Eligible Consumer Finance Accounts Receivable or Eligible Commercial Accounts Receivable in the ordinary course of business in connection with the collection or compromise thereof; and (J) dispositions of equipment that, in the aggregate during any 12-month period, has a fair market or book value (whichever is more) of \$500,000 or less).

(c) Indebtedness . No Issuer shall not create, incur, assume, guarantee, or be or remain liable with respect to any Indebtedness, other than the following:

(i) The Obligations;

(ii) Indebtedness under the Senior Credit Documents not to exceed \$20,000,000 in aggregate principal amount;

(iii) Funded Indebtedness of the Issuers existing as of the date of this Agreement and secured by the Permitted Liens disclosed on Schedule 7.2(c) to this Agreement, and all renewals, extensions, refundings, and refinancings of such Indebtedness in a principal amount that does not exceed the principal amount outstanding on the Closing Date;

(iv) Indebtedness for Taxes, assessments, or governmental charges to the extent that payment therefor shall at the time not be required to be made in accordance with Section 5.10 of this Agreement;

(v) Liabilities incurred by such Issuer in the ordinary course of business (not as a result of borrowing);

(vi) The endorsement of checks in the ordinary course of business;

(vii) Indebtedness incurred to refinance any Indebtedness permitted by this Section 7.2(c) of this Agreement;

(viii) Capital Leases and purchase money Indebtedness in an aggregate amount not to exceed \$1,000,000;

(ix) Intercompany Indebtedness existing as of the Closing Date to such Issuer's Subsidiaries in an aggregate amount not to exceed \$7,000,000 and intercompany Indebtedness to such Issuer's Subsidiaries involved exclusively in the Business in an amount not to exceed \$2,000,000 after the Closing Date;

(x) Indebtedness to an insurance company, the proceeds which are used by such Issuer to finance their insurance premiums payable on workers' compensation insurance policies maintained by such Issuer;

(xi) Indebtedness incurred in respect of the deferred purchase price for any acquisition of intellectual property or constituting the obligation to make purchase price adjustments in connection with any such acquisition of intellectual property;

(xii) Indebtedness that is not included in any of the preceding clauses of this Section, is not secured by a Lien and does not exceed \$5,000,000 in the aggregate at any time;

(xiii) Contingent obligations (A) arising from endorsements of payment items for collection or deposit in the ordinary course of business; (B) arising from any foreign currency hedging agreements not to exceed \$1,000,000 in the aggregate and not prohibited hereunder; (C) existing on the Closing Date and disclosed in writing to Purchasers, and any extension or renewal thereof that does not increase the amount of such contingent obligation when extended or renewed; (D) arising from customary indemnification obligations in favor of purchasers in connection with dispositions permitted under Section 7.2(b) hereof if such obligations could not reasonably be expected to have a Material Adverse Effect; or (E) Guaranties of Subsidiaries' Indebtedness that do not exceed \$1,000,000 in the aggregate and incurred in the ordinary course of business; and

(xiv) Reimbursement obligations to Bank of America, N.A. with respect to the letters of credit listed on Schedule 7.2(c).

(d) Restricted Payments . The Issuers shall not pay, make, declare, or authorize any Restricted Payment, redeem any Issuers' common stock or redeem, refinance, or otherwise dispose of or acquire any Issuers' preferred stock other than: (i) reasonable compensation paid to employees, officers, and directors in the ordinary course of business and consistent with prudent business practices; (ii) dividends to shareholders of any Issuer or dispositions to preferred shareholders of any Issuer declared as of the last day of a calendar quarter and paid in the immediately following calendar quarter and redemptions of common stock of any Issuer on the last day of a calendar quarter, provided that (A) no revolving loans are outstanding under the Senior Credit Agreement on the date such dividends and dispositions are declared and made and on the date such redemptions are made and (B) the aggregate amount of such dividends, dispositions, or redemptions (together with any other dividends, dispositions, and redemptions paid to shareholders of any Issuer during the 12 months ending on the such date) do not exceed (1) 50 percent of the Continuing Business Net Income for the 12 months ending on such date when the Debt to Tangible Net Worth Ratio is equal to or greater than 2.50 to 1.00 on such date, and (2) 100 percent of the Continuing Business Net Income for the 12 months ending on such date when the Debt to Tangible Net Worth Ratio is less than 2.50 to 1.00 on such date; (iii) conversion of preferred stock of Issuer to common stock of Issuer and (iv) any Subsidiary of the Issuer may declare and pay dividends to the Issuer.

(e) Investments; Purchase of Assets . The Issuers shall not make or maintain any Investments, or purchase or otherwise acquire any material amount of assets, other than:

(i) Purchases of Inventory in the ordinary course of business;

(ii) Purchases of intellectual property that do not exceed \$5,000,000 in the aggregate;

- (iii) Normal trade credit extended in the ordinary course of business and consistent with prudent business practice;
 - (iv) Capital Expenditures allowed under Section 7.2(l) of this Agreement;
 - (v) Investments in development of new product lines that are permitted under Section 7.2(i) of this Agreement;
 - (vi) Investment in Subsidiaries listed on Schedule 7.2(c) and Investments in Subsidiaries engaged exclusively in the Continuing Business made after the Closing Date that do not exceed \$5,000,000 in the aggregate;
 - (vii) Investment in joint ventures engaged exclusively in the Continuing Business made after the Closing Date that do not exceed \$5,000,000;
 - (viii) Loans and advances to officers and employees for salary, travel expenses, commissions and similar items in the ordinary course of business in the aggregate amount at any one time outstanding not to exceed \$500,000;
 - (ix) Payables permitted under Section 7.2(g) of this Agreement;
 - (x) The endorsement of instruments for collection or deposit in the ordinary course of business;
 - (xi) Stock or obligations issued to Issuer by any person (or the representative of such person) in respect of debt or other trade obligations of such person owing to Issuer in connection with the insolvency, bankruptcy, receivership or reorganization of such person or a composition, readjustment or settlement of the debts of such person or in respect of a settlement of a dispute with such person;
 - (xii) Investments in existence on the Closing Date set forth on Schedule 7.2(c).;
 - (xiii) Securities, instruments or other Investments that Issuer may acquire in connection with any disposition permitted hereunder; provided that such securities, instruments or other Investments shall constitute not more than 25 percent of the purchase price;
 - (xiv) Contingent obligations to the extent permitted under Section 7.2(c)(xiii).;
 - (xv) Foreign currency hedging agreements entered into in the ordinary course of business for non-speculative purposes in an aggregate amount not to exceed \$1,000,000;
 - (xvi) Loans to Subsidiaries of Issuer that are to be repaid within five Business Days of being made in an aggregate amount not to exceed \$8,000,000;
 - (xvii) Investments not otherwise permitted hereunder not to exceed \$1,000,000 at any one time, provided that no Default or Event of Default has occurred at the time of such Investments or would result therefrom; or
 - (xviii) Maintenance of deposits with Bank of the West or Investments in cash equivalents.
- (f) Obligations Relating to Guaranties . The Issuers shall not create, incur, assume or permit to exist any obligations arising under Guaranties except (i) by endorsement of instruments or items of payment for deposit to the general account of the Issuers, and (ii) for obligations arising under Guaranties incurred for the benefit of the Issuers if the primary obligation is expressly permitted by this Agreement.
- (g) Transactions with Affiliates . The Issuers shall not directly or indirectly enter into any purchase, sale, lease, sale-leaseback, or other transaction with any Affiliate, except transactions in the ordinary course of business on terms that are no less favorable to the Issuers than those that might be obtained at the time in a comparable arm's-length transaction with any Person that is not an Affiliate, provided, however, that the Issuers (i) may in any event enter into employment and severance arrangements with their respective officers and employees in the ordinary course of business, (ii) may engage in transactions with Affiliates expressly permitted in Section 7.2 hereof, (iii) may pay customary fees and reasonable out-of-pocket costs to, and indemnities provided on behalf of, directors, officers,

and employees in the ordinary course of business and (iv) may incur the Obligations under this Agreement and the other Purchase Documents.

(h) Fiscal Year and Accounting Changes . The Issuers shall not (i) change its fiscal year, or (ii) make any significant change (A) in accounting treatment and reporting practices (except as permitted by GAAP), or (B) in tax reporting treatment (except as required by law).

(i) Operations . The Issuers shall not engage in any activity or introduce any major product that is substantially different from or unrelated to the present business activities or products of the Issuers (other than any activities or products that are complimentary or ancillary to the present Business activities or products of the Issuers), or discontinue any portion of the Issuers' present business activities (other than the Business) that constitutes a substantial portion thereof.

(j) Prohibition on Change in Control . The Issuers shall not undergo a Change in Control.

(k) Subsidiaries . The Issuers shall not create or acquire any Subsidiary unless such Subsidiary is organized under the laws of the United States and becomes a party to and bound by, as a Co-Issuer, this Agreement.

(l) Capital Expenditures . The Issuers shall not make Capital Expenditures in any calendar year in excess of \$1,500,000 in the aggregate (the "Capital Expenditure Limitation"); provided, that in the event any Issuer does not expend the entire Capital Expenditure Limitation in any calendar year, such Issuer may carry forward 50 percent of such un-expended amount to the immediately succeeding calendar year. All Capital Expenditures shall first be applied to reduce the applicable Capital Expenditure Limitation and then to reduce the carry-forward from the previous calendar year, if any, provided that notwithstanding anything herein to the contrary, such Issuer shall not be entitled to carry forward any unutilized Capital Expenditure Limitation for more than one year.

ARTICLE 8

EVENTS OF DEFAULT

8.1 Event of Default . Any of the following shall constitute an "Event of Default":

(a) Non-Payment . The Issuers shall fail to pay any amount of principal (and such failure is not cured within three days) owed pursuant to the Notes when due, or the Issuers shall fail to pay any other amount payable by the Issuers under this Agreement or any other the Purchase Document when due (and such failure is not cured within 30 days); or

(b) Representation or Warranty . Any representation or warranty made by the Issuers under or in connection with this Agreement or any Purchase Document shall prove to have been incorrect in any material respect when made; or

(c) Specific Defaults . The Issuers shall fail to perform or observe (i) any covenant set forth in Section 7.1(a), Section 7.1(e) or Section 7.2, or (ii) any other covenant, obligation or term hereunder or under any of the Purchase Documents and such failure is not cured within 30 days of the earlier of the Requisite Purchasers' written notice thereof or the Issuers becoming aware of such failure; or

(d) Cross Default . The Issuers shall (i) fail to pay when due (after any applicable grace period) any amount payable in respect of any Indebtedness (including undrawn, committed, or available amounts and including amounts owing to all creditors under any combined or syndicated credit arrangement) exceeding \$1,000,000 in principal amount, unless the amount in question is subject to a bona fide dispute by such Issuer and has not been determined by a court, arbitrator, or other finder of fact to be owed by such Issuer, or (ii) fail to observe or perform (after any applicable notice or grace period) any term, covenant, or agreement evidencing or securing such Indebtedness, and the effect of such failure to observe or perform is to cause the acceleration of the maturity of such Indebtedness; provided, however, that no "Event of Default" which may occur under the Senior Credit Documents shall serve as a basis for the occurrence of an Event of Default hereunder unless the Senior Lender thereunder has accelerated the obligations under such Senior Loan Documents; or

(e) Insolvency; Voluntary Proceedings . The Issuers shall admit in writing its inability to pay its debts, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by such Issuer in any jurisdiction seeking to adjudicate such Issuer bankrupt or insolvent, or seeking reorganization, arrangement,

adjustment, or composition of such Issuer or such Issuer's debt under any law relating to bankruptcy, insolvency, or reorganization or relief of debtors, or seeking appointment of a receiver, trustee, or other similar official for such Issuer for such part of such Issuer's property as in the opinion of the Requisite Purchasers is a substantial part; or any such proceeding shall be instituted against such Issuer that is not dismissed within 60 days after the institution thereof, or such Issuer shall take any corporate action to authorize any of the actions set forth above in this Section 8.1(e); or any Governmental Authority shall declare or take any action that operates as a moratorium on the payment of debts of such Issuer; or

(f) Judgments . A judgment or order for the payment of money in excess of \$1,000,000 shall be entered against the Issuers or any of their Subsidiaries by any court, or a warrant of attachment or execution or similar process shall be issued or levied against property of Issuer or any of its Subsidiaries that in the aggregate exceeds \$1,000,000 in value, the payment of which is not fully covered by insurance in excess of any deductibles not exceeding \$100,000 in the aggregate, and such judgment, order, warrant, or process shall continue undischarged or unstayed or unbonded for 60 days; or

(g) Material Adverse Effect . Any occurrence or event that has a Material Adverse Effect; or

(h) Purchase Documents . Any material provision of any Purchase Document shall for any reason cease to be valid and binding on or enforceable against any Issuer party thereto or any Issuer shall so state in writing or bring an action to limit its obligations or liabilities thereunder.

8.2 Consequences of Event of Default .

(a) Bankruptcy and Cross-Acceleration . If an Event of Default specified in Section 8.1(e) hereof shall occur, the Accreted Value of the Notes and all other liabilities of the Issuers to the holders thereof hereunder and thereunder shall be immediately due and payable, without presentment, demand, protest or (except as expressly required hereby) notice of any kind, all of which are hereby expressly waived.

(b) Other Defaults . If any other Event of Default shall occur, Requisite Purchasers may at their option, by written notice to the Issuers, declare the entire unpaid balance of the Notes, and interest accrued thereon and all other liabilities of the Issuers here under and thereunder to be forthwith due and payable, and the same shall thereupon become immediately due and payable, without presentment, demand, protest or (except as expressly required hereby) notice of any kind, all of which are hereby expressly waived.

(c) Default Interest . Following the occurrence and during the continuance of any Event of Default, the holders of the Notes may at their option upon the election of the Requisite Purchasers, by written notice to the Issuers, declare, to the extent permitted by applicable law, that interest on the outstanding principal of, and premium and overdue interest, if any, on, the Notes shall accrue at a rate per annum equal to the interest rate thereon (determined as provided in Section 3.1 hereof) plus 200 basis points.

(d) Rights Not Exclusive . The rights provided for in this Agreement and the other Purchase Documents are cumulative and are not exclusive of any other rights, powers, privileges or remedies provided by law or in equity, or under any other instrument, document or agreement now existing or hereafter arising.

ARTICLE 9

MISCELLANEOUS

9.1 Successors and Assigns . This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns, except that (a) the Issuers may not assign or transfer its rights hereunder or any interest herein or delegate its duties hereunder and (b) Purchasers shall have the right to assign their rights hereunder and under the Notes in accordance with Article 6 hereof.

9.2 Modifications and Amendments . This Agreement may be amended, and the Issuers may take any action herein prohibited, or omit to perform any act herein required to be performed by it, if the Issuers shall obtain the prior written consent of the Requisite Purchasers to such amendment, action or omission to act; provided, however, that without the prior written consent of each Purchaser affected thereby, no such agreement shall (a) decrease the principal amount of, or, except as provided in Section 3.2 hereof, extend the maturity date of any Note, decrease the rate of interest on any Note (provided that a waiver of default interest shall not be deemed to decrease the rate

of interest), or decrease the amount payable by the Issuers in respect of the mandatory or optional redemption of any Note, (b) effect any waiver, amendment or modification that by its terms changes the amount or allocation of, or postpone or delay any date fixed for, any payment of principal, interest, fees or other amounts due to Purchasers pursuant to the Notes or any other Purchase Document, (c) amend the provisions of this Section 9.2 or the definition of the term "Requisite Purchasers", or (d) discharge the Issuers from their respective obligations under any Purchase Document. Each holder of a Note outstanding at the time of consent or times thereafter shall be bound by any consent authorized by this Section, whether or not such Note shall have been marked to indicate such consent.

9.3 No Implied Waivers; Cumulative Remedies; Writing Required . No delay or failure in exercising any right, power or remedy hereunder shall affect or operate as a waiver thereof; nor shall any single or partial exercise thereof or any abandonment or discontinuance of steps to enforce such a right, power or remedy preclude any further exercise thereof or of any other right, power or remedy. The rights and remedies hereunder are cumulative and not exclusive of any rights or remedies that Purchasers or any holder of Notes would otherwise have. Any waiver, permit, consent or approval of any kind or character of any breach or default under this Agreement or any such waiver of any provision or condition of this Agreement must be in writing and shall be effective only to the extent in such writing specifically set forth.

9.4 Reimbursement of Expenses . The Issuers upon demand shall pay or reimburse Purchasers for all reasonable fees and expenses incurred or payable by Purchasers (including, without limitation, reasonable fees and expenses of (x) not more than one firm of special counsel for Purchasers or (y) if such special counsel determines in good faith that such joint representation would constitute a conflict of interest, then not more than the number of firms of special counsel required to cure such conflict of interest), from time to time (a) arising in connection with the negotiation, preparation and execution of this Agreement, the Notes, the other Purchase Documents and all other instruments and documents to be delivered hereunder or thereunder or arising in connection with the transactions contemplated hereunder or thereunder, (b) relating to any amendments, waivers or consents pursuant to the provisions hereof or thereof, and (c) arising in connection with the enforcement of this Agreement or collection of the Notes. The amounts owed by the Issuers pursuant to this Section shall be paid by the Issuers in the ordinary course of the Issuers' business after the Purchasers bill the Issuers for such amounts, or on December 31, 2012, whichever occurs first.

9.5 Holidays . Whenever any payment or action to be made or taken hereunder or under the Notes shall be stated to be due on a day which is not a Business Day, such payment or action shall be made or taken on the next following Business Day, and such extension of time shall be included in computing interest or fees, if any, in connection with such payment or action.

9.6 Notices . All notices and other communications given to or made upon any party hereto in connection with this Agreement shall, except as otherwise expressly herein provided, be in writing (including telecopy, but in such case, a confirming copy will be sent by another permitted means) and mailed via certified mail, telecopied or delivered by guaranteed overnight parcel express service or courier to the respective parties, as follows:

to the Issuers :

Nautilus, Inc.

16400 S.E. Nautilus Drive

Vancouver, WA 98683

Attn: Alec Anderson

Email: aanderson@nautilus.com

with a copy (which shall not constitute notice to the Issuers) to:

Kirkland & Ellis LLP

300 N. LaSalle Street

Chicago, Illinois 60654

Attn: Jocelyn Hirsch

Email: Jocelyn.Hirsch@kirkland.com

to Purchasers :

As set forth on Annex A

or in accordance with any subsequent written direction from a party to the other parties. All such notices and other communications shall, except as otherwise expressly herein provided, be effective: upon delivery if delivered by courier or overnight parcel express service; in the case of certified mail, three (3) Business Days after the date sent; or in the case of telecopy, when received.

9.7 Survival . All representations, warranties, covenants and agreements of the Issuers contained herein or made in writing in connection herewith shall survive the execution and delivery of this Agreement and the purchase of the Notes and, except as otherwise provided herein, shall continue in full force and effect so long as any Note is outstanding and until payment in full of all of the Obligations hereunder or thereunder (other than contingent indemnification Obligations to the extent no claim giving rise thereto has been asserted). All obligations relating to indemnification or the reimbursement of expenses hereunder shall survive any termination of this Agreement and shall continue for the length of any applicable statute of limitations.

9.8 Governing Law . THIS AGREEMENT SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW YORK, WITHOUT REGARD TO CONFLICT OF LAWS PRINCIPLES.

9.9 Jurisdiction; Consent to Service of Process.

(a) EACH PARTY HERETO HEREBY IRREVOCABLY AND UNCONDITIONALLY SUBMITS, FOR ITSELF AND ITS PROPERTY, TO THE NONEXCLUSIVE JURISDICTION OF ANY NEW YORK STATE COURT OR FEDERAL COURT OF THE UNITED STATES OF AMERICA SITTING IN THE BOROUGH OF MANHATTAN IN THE STATE OF NEW YORK, AND ANY APPELLATE COURT FROM ANY THEREOF, IN ANY ACTION OR PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT, THE NOTES OR ANY OTHER PURCHASE DOCUMENT, OR FOR RECOGNITION OR ENFORCEMENT OF ANY JUDGMENT, AND EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY AND UNCONDITIONALLY AGREES THAT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, ALL CLAIMS IN RESPECT OF ANY SUCH ACTION OR PROCEEDING MAY BE HEARD AND DETERMINED IN SUCH NEW YORK COURT OR, TO THE EXTENT PERMITTED BY LAW, IN SUCH FEDERAL COURT. EACH OF THE PARTIES HERETO AGREES THAT A FINAL JUDGMENT IN ANY SUCH ACTION OR PROCEEDING SHALL BE CONCLUSIVE AND MAY BE ENFORCED IN OTHER JURISDICTIONS BY SUIT ON THE JUDGMENT OR IN ANY OTHER MANNER PROVIDED BY LAW. NOTHING IN THIS AGREEMENT SHALL AFFECT ANY RIGHT THAT PURCHASERS MAY OTHERWISE HAVE TO BRING ANY ACTION OR PROCEEDING RELATING TO THIS AGREEMENT, THE NOTES OR ANY OTHER PURCHASE DOCUMENT AGAINST THE ISSUER OR ITS PROPERTIES IN THE COURTS OF ANY JURISDICTION.

(b) EACH PARTY HERETO HEREBY IRREVOCABLY AND UNCONDITIONALLY WAIVES, TO THE FULLEST EXTENT IT MAY LEGALLY AND EFFECTIVELY DO SO, ANY OBJECTION THAT IT MAY NOW OR HEREAFTER HAVE TO THE LAYING OF VENUE OF ANY SUIT, ACTION OR PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT, THE NOTES OR ANY OTHER PURCHASE DOCUMENT IN ANY NEW YORK STATE COURT OR FEDERAL COURT LOCATED IN THE STATE OF NEW YORK. EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES, TO THE FULLEST EXTENT PERMITTED BY LAW, THE DEFENSE OF AN INCONVENIENT FORUM TO THE MAINTENANCE OF SUCH ACTION OR PROCEEDING IN ANY SUCH COURT.

(c) EACH PARTY TO THIS AGREEMENT IRREVOCABLY CONSENTS TO SERVICE OF PROCESS IN THE MANNER PROVIDED FOR NOTICES IN SECTION 9.6 HEREOF. NOTHING IN THIS AGREEMENT WILL AFFECT THE RIGHT OF ANY PARTY TO THIS AGREEMENT TO SERVE PROCESS IN ANY OTHER MANNER PERMITTED BY LAW.

9.10 Jury Trial Waiver . EACH PARTY HERETO HEREBY IRREVOCABLY WAIVE ANY RIGHT TO

TRIAL BY JURY IN ANY ACTION OR PROCEEDING (I) TO ENFORCE OR DEFEND ANY RIGHTS UNDER OR IN CONNECTION WITH THIS AGREEMENT, OR (II) ARISING FROM ANY DISPUTE OR CONTROVERSY IN CONNECTION WITH OR RELATED TO THIS AGREEMENT AND AGREES THAT ANY SUCH ACTION OR COUNTERCLAIM SHALL BE TRIED BEFORE A COURT AND NOT BEFORE A JURY.

9.11 Severability . Whenever possible, each provision of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision of this Agreement is held to be prohibited by or invalid under applicable law in any jurisdiction, such provision shall be ineffective only to the extent of such prohibition or invalidity, without invalidating any other provision of this Agreement.

9.12 Headings . Article, section and subsection headings in this Agreement are included for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

9.13 Indemnity . Each Issuer agrees to indemnify and hold harmless Purchasers, as well as Purchasers' shareholders, directors, officers, agents, attorneys, Subsidiaries, and Affiliates, from and against all damages, losses, settlement payments, obligations, liabilities, claims, suits, penalties, assessments, citations, directives, demands, judgments, actions, or causes of action, whether statutorily created or under the common law, all reasonable out-of-pocket costs and expenses (including, without limitation, attorneys' fees), and all other liabilities whatsoever that at any time or times shall be incurred, suffered, sustained, or required to be paid by any such indemnified Person (except any of the foregoing to the extent that they result from the bad faith, gross negligence or willful misconduct of any, indemnified Person) on account of, in relation to, or in any way in connection with any of the arrangements or transactions contemplated by, associated with, or ancillary to this Agreement, any of the other Purchase Documents, or any other documents executed or delivered in connection herewith or therewith, all as the same may be amended from time to time. In any investigation, proceeding, or litigation, or the preparation therefor, Purchasers shall select their own counsel and, in addition to the foregoing indemnity, each Issuer agrees to pay promptly the reasonable out-of-pocket fees and expenses of such counsel. In the event of the commencement of any such proceeding or litigation, each Issuer shall be entitled to participate in such proceeding or litigation with counsel of such Issuer's choice at such Issuer's own expense, provided that such counsel shall be satisfactory to Purchasers, in Purchasers' reasonable discretion. The provisions of this Section 9.13 of this Agreement shall survive payment (or satisfaction of payment) of all amounts owing with respect to the Notes or any other Purchase Document.

9.14 Counterparts . This Agreement may be executed in any number of counterparts and by any party hereto on separate counterparts, each of which, when so executed and delivered, shall be an original, but all such counterparts shall together constitute one and the same instrument.

9.15 Integration . This Agreement and the other Purchase Documents set forth the entire understanding of the parties hereto with respect to all matters contemplated hereby and supersede all previous agreements and understandings among them concerning such matters. No statements or agreements, oral or written, made prior to or at the signing hereof, shall vary, waive or modify the written terms hereof.

9.16 Subordination . THE OBLIGATIONS EVIDENCED HEREBY ARE SUBORDINATE, IN THE MANNER AND TO THE EXTENT SET FORTH IN THE SUBORDINATION AGREEMENT, TO THE INDEBTEDNESS AND OTHER LIABILITIES OWED BY THE ISSUERS UNDER AND PURSUANT TO THE SENIOR CREDIT DOCUMENTS, AND EACH PURCHASER HEREUNDER, BY ITS ACCEPTANCE HEREOF, ACKNOWLEDGES AND AGREES TO BE BOUND BY THE PROVISIONS OF THE SUBORDINATION AGREEMENT.

9.17 Confidentiality . Each of the Purchasers shall maintain in confidence in accordance with its customary procedures for handling confidential information and not disclose to any Person, all written or oral information that the Issuers or any of their Subsidiaries or any of their authorized representatives, furnishes to the Purchasers (" Confidential Information "), other than any such Confidential Information that becomes generally available to the public other than as a result of a breach by any Purchaser of its obligations hereunder or that is or becomes available to such Purchaser from a source other than the Issuers or any of their Subsidiaries, or any of their authorized representatives, and that is not, to the actual knowledge of the recipient hereof, subject to obligations of confidentiality with respect thereto; provided , however , that each Purchaser shall in any event have the right to deliver copies of any such documents, and to disclose any such information, to:

(a) Its Affiliates and to its and its Affiliates' directors, officers, trustees, partners, employees, agents, attorneys, professional consultants, portfolio management services (which services may be performed in the ordinary

course of such Purchaser's business as a financial institution by employees of such Purchaser's Affiliates on a need-to-know basis, provided such employees agree to keep such information confidential on the terms set forth in this Section 9.17.) and rating agencies;

(b) any other Purchaser;

(c) any Person to which such Purchaser offers to sell any Note or any part thereof or interest or participation therein (provided such Person agrees to keep such information confidential on the terms set forth in this Section 9.17.);

(d) any federal or state regulatory authority or examiner, or any insurance industry association, regulating or having jurisdiction over such Purchaser (upon prior written notice to the Issuers to the extent reasonably practicable and not prohibited by law or court order, so that the Issuers may, at their sole cost and expense, contest such disclosure or seek confidential treatment thereof; and provided that, with respect to disclosures to insurance industry agents, commercially reasonable efforts shall have been made to obtain the agreement of the party to whom such Confidential Information is being disclosed to be bound by the provisions of this Section 9.17.); and

(e) any other Person to which such delivery or disclosure may be necessary or appropriate (i) in compliance with any applicable law, rule, regulation or order, (ii) in response to any subpoena or other legal process or informal investigative demand, (iii) in connection with any litigation with respect to this Agreement or the other Purchase Documents to which such Purchaser is a party, or (iv) in connection with the enforcement of the rights and remedies of the Purchasers under this Agreement and the other Purchase Documents at any time when an Event of Default shall have occurred and be continuing (with respect to clauses (i), (ii) and (iii) of this Section 9.17(e).), in each case upon prior written notice to the Issuers to the extent reasonably practicable and not prohibited by law or court order, so that the Issuers may, at their sole cost and expense, contest such disclosure or seek confidential treatment thereof.

In any event, however, the Issuers and each Purchaser may disclose to any and all Persons, without limitation of any kind, the tax treatment and tax structure of the transactions contemplated hereby and all materials of any kind (including opinions or other tax analyses) that are provided to any Purchaser relating to such tax treatment and tax structure; it being understood that this authorization is retroactively effective to the commencement of the first discussions between or among any of the parties regarding the transactions contemplated hereby.

9.18 Waiver of Consequential Damages . To the fullest extent permitted by applicable law, each Issuer hereby agrees not to assert, and each Issuer hereby waives, any claim against any indemnitee under Section 9.13 of this Agreement on any theory of liability for special damages, indirect damages, consequential damages, or punitive damages (as opposed to direct or actual damages) arising out of, in connection with, or as a result of, this Agreement, any other Purchase Document, or any agreement or instrument contemplated hereby, the transactions contemplated hereby or thereby, any Note, or the use of the proceeds thereof.

9.19 Payments Set Aside . To the extent any payments in respect of the Notes (including, but not limited to, any proceeds received by the Purchasers as a result of any enforcement proceeding or setoff), or any part thereof, subsequently are invalidated, declared to be fraudulent or preferential, set aside, or required to be repaid to a trustee, receiver, or any other Person under any law or equitable cause, then, to the extent of such repayment (including any such repayment made voluntarily by the Purchasers in their reasonable discretion), the Notes or part thereof originally intended to be satisfied, and all rights and remedies therefor, shall be revived and shall continue in full force and effect, and the Purchasers' rights, powers, and remedies under this Agreement and the Purchase Documents shall continue in full force and effect, as if such payment had not been made, or such enforcement proceeding or setoff had not occurred. In such event, each Purchase Document automatically shall be reinstated and the Issuers shall take such action as reasonably may be requested by the Purchasers to effect such reinstatement.

9.20 No Duties Among Purchasers . Notwithstanding anything to the contrary contained herein or in any other Purchase Document, including, without limitation, the Subordination Agreement, no Purchaser shall owe any duty, fiduciary or otherwise, to any other Purchaser.

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Note Purchase Agreement

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SIGNATURE PAGE TO

NOTE PURCHASE AGREEMENT

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

ISSUER :

- **NAUTILUS, INC.,**
a Washington corporation

By: /s/ Kenneth Fish

Name: Kenneth Fish

Title: Chief Financial Officer

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- **Note Purchase Agreement**

SIGNATURE PAGE TO

NOTE PURCHASE AGREEMENT

PURCHASER:

Sherborne Strategic Fund A, LLC

By: /s/ Craig L. McKibben

Name: Craig L. McKibben

Title: Managing Director,

Sherborne Investors LP as Managing Member

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Note Purchase Agreement

SIGNATURE PAGE TO
NOTE PURCHASE AGREEMENT

PURCHASER:

Nottingham Investors LLC

By: /s/ Craig L. McKibben

Name: Craig L. McKibben

Title: Managing Director

Sherborne Investors LP as Managing Member

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Note Purchase Agreement

ANNEX A

TO

NOTE PURCHASE AGREEMENT

Purchaser and Payment Information

INVESTMENT INFORMATION:

-	-	-	-	-
-	-	-	-	-
-	-	-	-	-
<u>Purchaser</u>	<u>Pro Rata</u>	<u>Investment</u>	<u>Pro Rata</u>	<u>Portion of</u>
				<u>the Notes</u>
Sherborne Strategic Fund A, LLC	8.51	%	\$	425,600.00
Sherborne Strategic Fund B, LLC	12.85	%		642,550.00
		%<		
Nottingham Investors LLC	78.64/div>			3,931,850.00
-	100.00	%	\$	5,000,000.00

Notices for each of the Purchasers should be sent to such Purchaser at the following address:

c/o Sherborne Investors LP

135 East 57th Street

New York, NY 10022

Annex A to

Note Purchase Agreement

Payment and Notice Instructions

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Schedule 5.5

Litigation

None.

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Note Purchase Agreement

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Schedule 7.2(a)

Liens

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Note Purchase Agreement

<u>FILING TYPE</u>	<u>FILE NUMBER & DATE</u>	<u>DEBTOR</u>	<u>SECURED PARTY</u>	<u>COLLATERAL DESCRIPTION</u>
UCC	200631958040 11/15/06	NAUTILUS, INC. 16400 SE NAUTILUS DR. Vancouver, WA	NMHG Financial Services, Inc. 10 Riverview Drive Danbury, CT	Leased equipment.
UCC	200632676363 11/22/06	NAUTILUS, INC. 16400 SE NAUTILUS DR. Vancouver, WA	Raymond Leasing Corporation 20 S. Canal Street Greene, NY	Specific equipment.
UCC	200632676370 11/22/06	Nautilus, Inc. 16400 SE NAUTILUS DR. Vancouver, WA	Raymond Leasing Corporation 20 S. Canal Street Greene, NY	Specific equipment.
UCC	200633800866 12/1/06	Nautilus, Inc. 16400 SE NAUTILUS DR. Vancouver, WA	Raymond Leasing Corporation 20 S. Canal Street Greene, NY	Specific equipment.
UCC	200719346035 7/12/07	NAUTILUS INC 16400 SE NAUTILUS DR. Vancouver, WA	US Bancorp 1310 Madrid Street Marshall, MN	For informational purposes: Specific equipment.
UCC	200719346042 7/12/07	NAUTILUS INC 16400 SE NAUTILUS DR. Vancouver, WA	US Bancorp 1310 Madrid Street Marshall, MN	For informational purposes: Specific equipment.
UCC	200720065482 7/19/07	NAUTILUS INC 16400 SE NAUTILUS DR. Vancouver, WA	US Bancorp 1310 Madrid Street Marshall, MN	For informational purposes: Specific equipment.
UCC	200724802953 9/5/07	NAUTILUS INC 16400 SE NAUTILUS DR. Vancouver, WA	US Bancorp 1310 Madrid Street Marshall, MN	For informational purposes: Specific equipment.
UCC	200730683140 11/2/07	Nautilus, Inc. 16400 SE NAUTILUS DR. Vancouver, WA	Raymond Leasing Corporation 20 S. Canal Street Greene, NY	Specific equipment.
UCC	200801177264 1/11/08	NAUTILUS INC 16400 SE NAUTILUS DR. Vancouver, WA	US Bancorp 1310 Madrid Street Marshall, MN	For informational purposes: Specific equipment.
UCC	200804573155 2/14/08	NAUTILUS INC 16400 SE NAUTILUS DR. Vancouver, WA	US Bancorp 1310 Madrid Street Marshall, MN	For informational purposes: Specific equipment.
UCC	200819299651 7/10/08	Nautilus, Inc. 16400 SE Nautilus Dr Vancouver, WA	ABS Finance PO BOX 609 CEDAR RAPIDS, IA	For informational purposes: Leased equipment.
	200820427944 7/22/08			
<u>FILING TYPE</u>	<u>FILE NUMBER & DATE</u>	<u>DEBTOR</u>	<u>SECURED PARTY</u>	<u>COLLATERAL DESCRIPTION</u>
UCC		Nautilus Inc. 16400 SE Nautilus Dr Vancouver, WA	CIT Technology Financing Services, Inc. 10201 Centurion Parkway North Suite 100 Jacksonville, FL	For informational purposes: Leased equipment.

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-	-	-	-	-	-	-	-	-	-
							<u>Additional</u>		
							<u>Secured Party:</u>		
							<u>ABS</u>		
							<u>Finance</u>		
							<u>7440 SW</u>		
							<u>Bonita Rd</u>		
-	-	-	-	-	-	-	<u>Portland, OR</u>	-	-
-	-	-	-	-	-	-	-	-	-
							<u>Wells Fargo</u>		
							<u>Bank, N.A.</u>		
							<u>300 Tri State</u>		
							<u>International</u>		
		<u>200903519672</u>					<u>Ste 400</u>		
		<u>2/4/09</u>					<u>Lincolnshire,</u>		
<u>UCC</u>	-	-	-	<u>VA</u>		<u>IL</u>		-	<u>Specific</u>
-	-	-	-	-	-	-	-	-	<u>equipment.</u>
							<u>Virginia</u>		
							<u>Business Systems Inc.</u>		
							<u>PO Box 609</u>		
							<u>Cedar</u>		
		<u>200903628251</u>					<u>Rapids, IA</u>	-	<u>Leased</u>
<u>UCC</u>	-	<u>2/5/09</u>	-	<u>VA</u>	-	-		-	<u>equipment.</u>
-	-	-	-	-	-	-	-	-	-
							<u>Bank of the</u>		
							<u>West</u>		
							<u>222 SW</u>		
							<u>Columbia Street,</u>		
							<u>Suite 1200</u>		
<u>UCC</u>	-	<u>201006776207</u>	-	<u>WA</u>	-	-	<u>Portland, OR</u>	-	<u>All assets of</u>
-	-	<u>03/08/2010</u>	-	-	-	-	-	-	<u>Debtor, whether or not</u>
									<u>owed or acquired.</u>
									-
							<u>GE Money.</u>		
							<u>Bank</u>		
							<u>170 Election</u>		
							<u>Road, Suite 125</u>		
<u>UCC</u>	-	<u>201018384704</u>	-	<u>WA</u>	-	-	<u>Draper, UT</u>	-	<u>Lien pursuant to</u>
-	-	<u>07/01/2010</u>	-	-	-	-		-	<u>the Private Label</u>
									<u>Consumer Credit Card</u>
									<u>Program Agreement</u>

2. Letter of Credit in the amount of \$1,945,386 issued by Bank of America

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Schedule 7.2(c)

Indebtedness

1. Indebtedness evidenced by Senior Credit Documents

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2. Letter of Credit in the amount of \$1,945,386 issued by Bank of America

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Note Purchase Agreement

EXECUTION COPY

SUBORDINATION AGREEMENT

This SUBORDINATION AGREEMENT (this "Agreement") is made and entered into as of September 3, 2010, by BANK OF THE WEST, a California state chartered bank, and its successors and assigns (the "Senior Creditor"), and Sherborne Strategic Fund A, LLC, a Delaware limited liability company, Sherborne Strategic Fund B, LLC, a Delaware limited liability company and Nottingham Investors LLC, a Delaware limited liability company, (collectively the "Subordinated Creditors" and each individually a "Subordinated Creditor").

1. Definitions.

"Adjusted Continuing Business EBITDA" shall have the meaning given to such term in the Senior Loan Agreement.

"Bankruptcy Code" shall mean Title 11, United States Code, or any similar Federal, state or foreign law for the relief of debtors.

"Borrower" shall mean Nautilus, Inc., a Washington corporation, and any successor issuer of indebtedness under the Senior Loan Agreement.

"Collateral" shall have the meaning given to such term in the Senior Loan Agreement.

"Conforming Amendment" shall mean any amendment to a provision of any Subordinated Document that is substantively identical to a corresponding amendment to a comparable provision of a Loan Document.

"Enforcement Action" shall mean (a) to take from or for the account of Borrower by set-off or in any other manner, the whole or any part of any moneys which may now or hereafter be owing by Borrower with respect to any of the Subordinated Indebtedness not otherwise permitted under Paragraphs 3 or 5 hereof, (b) to sue for payment of or to initiate or participate with others in any suit, action or proceeding against Borrower to (i) enforce payment of or to collect the whole or any part of the Subordinated Indebtedness (including, without limitation, any Permitted Payment) or (ii) commence judicial enforcement of any of the rights and remedies under any of the Subordinated Documents or applicable law with respect to any of the Subordinated Indebtedness, (c) to accelerate any of the Subordinated Indebtedness or (d) to exercise any put option or to cause Borrower to honor any redemption or mandatory prepayment obligation under any Subordinated Document; provided that the following shall not be considered an "Enforcement Action": (i) to seek specific performance or other injunctive relief to compel Borrower to comply with an obligation under the Subordinated Documents so long as it is not accompanied by a claim for monetary damages or for payment of any of the Subordinated Indebtedness, (ii) to take any action necessary to prevent the running of any applicable statute of limitations or similar restriction on claims which has not been waived by the Borrower or cannot be waived as a matter of law so long as any amounts paid to or for the benefit of the Subordinated Creditors as a result of any such action are immediately paid over to the Senior Creditor for application against the Senior Indebtedness as provided in Paragraph 6 herein or (iii) any action necessary solely to assert a compulsory cross-claim or counterclaim against the Borrower.

"Event of Default" shall have the meaning set forth in the Subordinated Notes or the other Subordinated Documents or any other agreement, document or instrument evidencing, securing or guaranteeing the payment of or otherwise relating to any of the Subordinated Indebtedness.

"First Amendment" shall mean that certain First Amendment of Credit Agreement between Borrower and Senior Creditor dated as of August 13, 2010, amending the Senior Loan Agreement.

"Loan Documents" shall have the meaning given to such term in the Senior Loan Agreement.

"Majority Subordinated Creditors" shall mean the Subordinated Creditors holding greater than 50% of the aggregate principal amount at maturity of the Subordinated Notes then outstanding.

"Paid in Full" shall mean (a) paid in full in cash (other than unasserted contingent indemnification obligations as to which no claim is known or determinable) and (b) the termination or cash collateralization (in

an amount and in the manner required by the Senior Loan Agreement) of all Letters of Credit (as defined in the Senior Loan Agreement) issued under the Senior Loan Agreement.

"Permitted Payments" shall have the meaning ascribed to such term in Paragraph 3(b) herein.

"Proceeding" shall have the meaning ascribed to such term in Paragraph 5 herein.

"Quarterly Adjusted Continuing Business EBITDA" means, for any calendar quarter, the Adjusted Continuing Business EBITDA for the four quarters ending on the last day of such quarter.

"Senior Debt Cap" shall mean the result of (a) \$20,000,000, plus (b) interest, fees, expenses and all other amounts that are capitalized pursuant to the terms of the Senior Loan Agreement.

"Senior Indebtedness" shall mean the sum of (a) any and all indebtedness (principal, interest, fees, collection costs and expenses and other amounts), liabilities and obligations which Borrower may now or at any time or times hereafter owe to the Senior Creditor, and/or its successors and assigns, evidenced by or arising under the Senior Loan Agreement or Senior Note; provided that Senior Indebtedness shall not include the principal balance of any loans or undrawn amounts of outstanding letters of credit issued under the Senior Loan Agreement in excess of the Senior Debt Cap and any portion of interest and fees accrued on account of such portion of loans and letters of credit.

"Senior Loan Agreement" shall mean that certain Credit Agreement dated as of March 8, 2010, between Borrower and the Senior Creditor, as amended by the First Amendment, and any further amendments, modifications, extensions, refinancings, restatements and renewals thereof to the extent not prohibited by this Agreement.

"Senior Note" shall mean that certain promissory note of Borrower dated as of March 8, 2010, payable to the order of Senior Creditor in the principal amount of \$15,000,000 and any additions, increases, amendments, modifications, extensions, refinancings, replacements and renewals thereof to the extent not prohibited by this Agreement.

"Subordinated Creditors" shall have the meaning ascribed to such term in the preamble hereto.

"Subordinated Documents" shall mean the Subordinated Notes and any and all other agreements, documents and instruments heretofore, now or hereafter delivered to the Subordinated Creditors with respect to or in connection with or pursuant to the Subordinated Notes or any loans or advances made pursuant thereto.

"Subordinated Indebtedness" shall mean any and all indebtedness (principal, interest, fees, collection costs and expenses and other amounts), liabilities and obligations (including, without limitation, guaranty obligations and indemnity obligations) which Borrower may now or at any time or times hereafter owe to the Subordinated Creditors pursuant to the Subordinated Documents.

"Subordinated Notes" shall mean one or more promissory notes in the aggregate principal amount at maturity of \$6,096,996.21 from Borrower to the Subordinated Creditors and any additions, increases, amendments, modifications, extensions, refinancings, replacements and renewals thereof to the extent not prohibited by this Agreement.

"Subordinated Securities" shall mean any securities of Borrower issued in connection with a Proceeding involving Borrower, the payment of which securities is junior or otherwise subordinated, at least to the same extent provided in this Agreement, to the payment of any and all of the Senior Indebtedness.

2. Subordination. To induce the Senior Creditor to now or hereafter lend or advance monies or otherwise extend credit to or for the benefit of Borrower, and to better secure the Senior Creditor in respect thereof, each Subordinated Creditor agrees to and hereby subordinates on the terms and conditions contained herein the payment and performance of all of the Subordinated Indebtedness together with any and all guaranties, collateral and other security, if any, for the payment of any of the Subordinated Indebtedness, to any and all of the Senior Indebtedness until the Senior Indebtedness is Paid in Full and the Senior Creditor has no further commitment to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document.

3. Permitted Payments.

(a) General Prohibition of Payments on Subordinated Indebtedness . Each Subordinated Creditor covenants and agrees with the Senior Creditor that, except as specifically permitted under Paragraph 3(b), Borrower shall not pay, and no Subordinated Creditor shall accept payment of, any of the Subordinated Indebtedness or any guaranties, unless and until all of the Senior Indebtedness has been Paid in Full and the Senior Creditor has no further commitments to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document.

(b) Permitted Payments . Until such time as all of the Senior Indebtedness has been Paid in Full, Borrower may pay to the Subordinated Creditors, and the Subordinated Creditors may accept from the Borrower (collectively, the "Permitted Payments") only:

(i) Any payments of interest with respect to the Subordinated Indebtedness that are paid "in kind," whether capitalized and added to then outstanding principal amount of the Subordinated Indebtedness or accrued or accreted as unpaid interest so long as such payments "in kind" do not become obligations for payment of cash, securities or any other form of payment (other than in each case in the form of Subordinated Securities) until the earlier of (x) after all of the Senior Indebtedness has been Paid in Full or (y) the scheduled maturity date of the Subordinated Indebtedness (it being acknowledged and agreed by the Subordinated Creditors that such scheduled maturity date will be automatically extended (without any action by the Borrower or any Subordinated Creditor) by a number of days that the maturity date of the Senior Indebtedness is extended provided that such scheduled maturity date may not be extended by more than 180 days without the consent of each Subordinated Creditor);

(ii) Payment of all or any portion of principal or interest on the Subordinated Indebtedness, so long as on the date of any proposed payment, (x) Quarterly Adjusted Continuing Business EBITDA for the two immediately preceding calendar quarters was greater than \$5,000,000 for each such quarter, (y) Borrower is in compliance with all covenants and requirements set forth in the Senior Loan Agreement without giving effect to the amendments to the Senior Loan Agreement set forth in Section 4 of the First Amendment, and (z) no default or event of default exists under the Senior Loan Agreement or any other Loan Document, and no default would occur under the Senior Loan Agreement or any other Loan Document as a result of such payment;

(iii) Payments of principal and accreted or accrued interest upon the occurrence of a Change in Control (as defined in the Subordinated Documents as in effect on the date hereof) and the declaration of an "Event of Default" under the Subordinated Documents in accordance with the terms thereof, but only to the extent that the Senior Creditor has consented in writing to such Change in Control or has waived (or agreed to forbear from exercising remedies in connection with) in writing any Event of Default under the Loan Documents that may have occurred as a result of such Change in Control; and

(iv) Reimbursement of reasonable out-of-pocket costs and expenses (including without limitation, attorney fees) due and owing to any Subordinated Creditor;

provided, in the case of clauses (iii) and (iv) only if such payments are payments made in accordance with the terms of the Subordinated Documents as in effect on the date hereof or as modified in accordance with the terms of this Agreement.

4. Enforcement Rights of Subordinated Creditor.

(a) Limitation on Right of Action . Except as expressly set forth in Paragraph 4(b), the Subordinated Creditors shall have no right to accelerate the maturity of any of the Subordinated Indebtedness or take any other Enforcement Action, unless and until all of the Senior Indebtedness has been Paid in Full and the Senior Creditor has no further commitment to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document.

(b) Standstill . Until the Senior Indebtedness is Paid in Full and the Senior Creditor has no further commitment to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document, no Subordinated Creditor shall, without the prior written consent of the Senior Creditor, take any Enforcement Action permitted under the Subordinated Notes, the Subordinated Documents and/or applicable law, until the earliest to occur of the following:

(i) acceleration of the Senior Indebtedness; or

(ii) the commencement of a Proceeding; or

(iii) the commencement by the Senior Creditor of any judicial or non-judicial action or proceeding against Borrower to realize upon any Collateral owned by Borrower securing the Senior Indebtedness;

(iv) upon the occurrence of a "Change in Control" under the Subordinated Documents to the extent the payment of the Subordinated Indebtedness would be permitted by Paragraph 3(b)(iii) of this Agreement; or

(v) the passage of 180 days from the delivery by the Majority Subordinated Creditors to the Senior Creditor of a written notice stating that an Event of Default (other than as described in clause (iv) above) has occurred under the Subordinated Indebtedness and the Majority Subordinated Creditors desire to take an Enforcement Action against Borrower as a consequence thereof (any such notice being hereinafter referred to as a "Subordinated Debt Default Notice"); provided that the Event of Default under the Subordinated Notes described in such Subordinated Debt Default Notice shall not have been cured or waived within such 180-day period, and provided further, the Senior Creditor shall have received 10 days prior written notice of the Majority Subordinated Creditors' intention to take any such Enforcement Action (such 10-day notice period may run concurrently with the 180-day period required under this clause (v)).

Any such Enforcement Action by the Subordinated Creditors shall remain subject to and subordinated to any Enforcement Actions by the Senior Creditor with respect to the Senior Indebtedness against Borrower or any property or assets of Borrower, and any amounts received by the Subordinated Creditors from any such Enforcement Action shall be promptly turned over to the Senior Creditor as provided in Paragraph 6 until the Senior Indebtedness has been Paid in Full. Nothing herein shall be construed in any way to limit or impair the right of the Senior Creditor to bid for and purchase Collateral at any private or judicial foreclosure upon such Collateral initiated by the Senior Creditor. The provisions of this Agreement shall continue in full force and effect notwithstanding the occurrence of a Proceeding. Notwithstanding the foregoing, the Subordinated Creditors may file proofs of claim and make other filings against Borrower in any Proceeding involving Borrower.

(c) Rescission of Senior Defaults . Notwithstanding anything contained herein to the contrary, if following the acceleration of the Senior Indebtedness such acceleration is rescinded (whether or not any existing event of default under the Senior Loan Agreement or other Loan Documents has been cured or waived), then all Enforcement Actions taken by the Subordinated Creditors shall likewise be rescinded if such Enforcement Action is based solely on clause (i) of Paragraph 4(b). Notwithstanding anything contained herein to the contrary, if following commencement of any judicial or non-judicial action or proceeding against Borrower to realize upon any Collateral owned by Borrower securing the Senior Indebtedness such judicial or non-judicial action or proceeding is subsequently terminated or rescinded (whether or not any existing event of default under the Senior Loan Agreement or other Loan Documents has been cured or waived), then all Enforcement Actions taken by the Subordinated Creditors shall likewise be terminated or rescinded if such Enforcement Action is based solely on clause (iii) of Paragraph 4(b).

5. Insolvency . In the event Borrower makes any assignment or other arrangement for the benefit of its creditors or any bankruptcy, receivership, reorganization, dissolution, insolvency or other similar proceeding is filed or otherwise initiated by, against or involving Borrower (a "Proceeding"), (a) all of the Senior Indebtedness shall be Paid in Full before any payment shall be made on or with respect to any of the Subordinated Indebtedness (other than any payment in the form of Subordinated Securities), and (b) any payment which, but for the terms of this Agreement, would be payable or deliverable on or in respect of any of the Subordinated Indebtedness (other than in the form of Subordinated Securities) shall be paid or delivered directly to the Senior Creditor to be applied as a payment on the Senior Indebtedness until (i) all of the Senior Indebtedness has been Paid in Full and (ii) the Senior Creditor has no further commitments to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document. Each Subordinated Creditor hereby irrevocably authorizes, empowers and directs all receivers, trustees, liquidators, custodians, conservators and others having authority in the premises to make any such payments or distributions directly to the Senior Creditor and the Subordinated Creditors further irrevocably authorizes and empowers the Senior Creditors to demand, sue for, collect and receive each and every such payment or distribution. Each Subordinated Creditor hereby agrees to execute and deliver to the Senior Creditor or any of its representatives all such further agreements, documents and instruments as may from time to time be reasonably requested by the Senior Creditor confirming the authorizations referred to in the foregoing clause (b). Each Subordinated Creditor hereby further irrevocably authorizes, empowers and appoints the Senior Creditor as its agent and attorney-in-fact to execute, verify, deliver and file such proofs of claim in respect of Subordinated Indebtedness in connection with such Proceeding if the

Subordinated Creditors fail to do so on or before the date that is five days prior to the bar date for filing such proofs of claim.

Each Subordinated Creditor agrees that the Senior Creditor may consent to the use of cash collateral to provide financing to Borrower on such terms and conditions and in such amounts as the Senior Creditor, in its sole discretion, may decide and that no Subordinated Creditor shall contest or oppose in any manner, such cash collateral use or financing; provided that the amount of such financing plus the amounts outstanding under the Senior Loan Agreement shall not exceed the Senior Debt Cap. Borrower (or a trustee appointed for the estate of Borrower) may grant to the Senior Creditor liens upon all or any part of the assets of Borrower, which liens (i) shall secure payments of all or any part of the Senior Indebtedness (whether such Senior Indebtedness arose prior to the filing of the petition for relief or arise thereafter); and (ii) shall be superior in priority to the liens on the assets of Borrower held by the Subordinated Creditors. Each Subordinated Creditor agrees that it will not object to or oppose (A) a sale or other disposition of any assets securing the Senior Indebtedness (or any portion thereof) free and clear of liens or other claims under Section 363 of the Bankruptcy Code (11 U.S.C. Section 101, *et. seq.*) or any other provision of the Bankruptcy Code if the Senior Creditor has consented to such sale or disposition of such assets, or (B) a plan of reorganization or liquidation pursuant to chapter 11 of the Bankruptcy Code if the Senior Creditor has voted to accept such plan of reorganization or liquidation. Each Subordinated Creditor covenants and agrees that it will not obtain, seek to obtain or accept any security or collateral for any of the Subordinated Indebtedness without the prior written consent of the Senior Creditor. In the event that the Senior Creditor gives prior written consent to the Subordinated Creditors to obtain security or collateral for any Subordinated Indebtedness and the Subordinated Creditors obtain security or collateral for any Subordinated Indebtedness, then (1) each Subordinated Creditor agrees that it will obtain such security or collateral only with respect to the assets of Borrower specifically identified by the Senior Creditor in such prior written consent and only with respect to such Subordinated Indebtedness specifically identified by the Senior Creditor in such prior written consent and (2) each Subordinated Creditor agrees not to assert any right it may have to "adequate protection" of its interest in such security or collateral in any Proceeding and agrees that it will not seek to have the automatic stay lifted with respect to such security or collateral, without the prior written consent of the Senior Creditor. Each Subordinated Creditor waives any claim it may now or hereafter have arising out of the Senior Creditor's election, in any Proceeding, of the application of Section 1111(b)(2) of the Bankruptcy Code, and/or any borrowing or grant of a security interest under Section 364 of the Bankruptcy Code by Borrower, as debtor in possession. Each Subordinated Creditor (both in its capacity as a Subordinated Creditor and in its capacity as a party which may be obligated to Borrower with respect to contracts which are part of the Senior Creditor's Collateral) agrees not to initiate or prosecute or encourage any other person to initiate or prosecute any claim, action or other proceeding (a) challenging the enforceability of the Senior Creditor's claims or oppose any action by the Senior Creditor to enforce its rights or remedies relating to any of the Senior Indebtedness, (b) challenging the enforceability, validity, priority or perfected status of any liens on assets securing any of the Senior Indebtedness or (c) asserting any claims which Borrower may hold with respect to the Senior Creditor. Until the discharge of all of the Senior Indebtedness has occurred, the Subordinated Creditors shall not seek relief from the automatic stay without the prior written consent of the Senior Creditor or oppose any request by the Senior Creditor to seek relief from the automatic stay with respect to the Collateral.

6. Turnover of Payments . Each Subordinated Creditor hereby agrees that if any payment or payments are made to or accepted by any Subordinated Creditor in violation of this Agreement , such Subordinated Creditor will promptly, after its becoming aware thereof, deliver all such payments to the Senior Creditor, with any necessary endorsement of such Subordinated Creditor, as a payment on the Senior Indebtedness. In the event that such Subordinated Creditor turns over or delivers to the Senior Creditor any amount paid to such Subordinated Creditor on account of the Subordinated Indebtedness, the obligations of Borrower under the Subordinated Notes and the other Subordinated Documents with respect thereto shall be revived and continued as Subordinated Indebtedness in full force and effect, as if such amount or property has not been paid or received.

7. Subrogation . After all of the Senior Indebtedness is Paid in Full and the Senior Creditor has no further commitment to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document, the Subordinated Creditors shall be subrogated to the rights of the Senior Creditor (to the extent of any payments made on the Subordinated Indebtedness which were applied to the Senior Indebtedness under Paragraphs 3, 4, 5, 6 or otherwise) to receive payments or distributions of assets of Borrower applicable to the Senior Indebtedness until the principal of, and interest and premium, if any, on, and all other amounts payable in respect of the Subordinated Indebtedness shall be paid in full. For purposes of preserving such subrogation rights, payments of the Subordinated Indebtedness to which the Subordinated Creditors would have been entitled but for the provisions of this Agreement, which are paid pursuant to the provisions of this Agreement to the Senior

Creditor for application to the Senior Indebtedness by the Subordinated Creditors, as among Borrower and its creditors (other than the Senior Creditor), shall not be deemed to be a payment by Borrower to or on account of the Senior Indebtedness.

8. Amendments.

(a) Each Subordinated Creditor agrees that none of the Subordinated Documents or any other document, instrument, or agreement evidencing all or any part of the Subordinated Indebtedness may be amended, restated, supplemented, refinanced, or otherwise modified, without the prior written consent of the Senior Creditor, except to the extent that the effect of such amendment, restatement, supplement, refinancing or other modification is to (i) increase the rate of interest (whether payable in cash or in-kind) on any of the Subordinated Notes to a rate not in excess of 2.00% per annum above the interest rate set forth in the Subordinated Document (as in effect on the date hereof), except in connection with the imposition of a default rate of interest in accordance with the terms of the Subordinated Documents (as in effect on the date hereof) (which shall be governed by clause (ii) below), or (ii) increase the default rate of interest (whether payable in cash or in kind) on any of the Subordinated Notes to a rate not in excess of 3.00% per annum above the interest rate set forth in the Subordinated Documents (as in effect on the date hereof); provided, that any Conforming Amendment to the Subordinated Documents may be made so long as such Conforming Amendment shall maintain an equivalent proportionate difference between dollar amounts in the relevant provision in the Subordinated Documents and those in the corresponding covenant in the Senior Loan Agreement, to the extent that such difference exists between the Subordinated Documents and the Senior Loan Agreement on the date hereof.

(b) The Senior Creditor may at any time and from time to time without the consent of or notice to any Subordinated Creditor, without incurring liability to any Subordinated Creditor and without impairing or releasing the obligations of any Subordinated Creditor under this Agreement, change the manner or place of payment or extend the time of payment of or renew or alter any of the terms of the Senior Indebtedness, or amend in any manner any agreement, note, guaranty or other instrument evidencing or securing or otherwise relation to the Senior Indebtedness; provided that Senior Creditor will not, without the prior written consent of the Majority Subordinated Creditors, acting on behalf of all Subordinated Creditors, agree to any amendment, modification or supplement to the Loan Documents, the effect of which is to (i) increase the maximum principal amount of the Senior Indebtedness to an amount in excess of the Senior Debt Cap, (ii) increase the interest rate margins or any fixed interest rate with respect to the Senior Indebtedness by more than 3.00% per annum above the interest rate contained in the Senior Loan Agreement (as in effect on the date hereof), except in connection with the imposition of a default rate of interest, in each case, in accordance with the terms of the Loan Documents (as in effect on the date hereof), (iii) increase the default rate of interest (whether payable in cash or in kind) on any of the Senior Indebtedness to a rate in excess of 3.00% per annum above the interest rate set forth in the Senior Loan Agreement (as in effect on the date hereof), (iv) modify or add any covenant or "Event of Default" under the Loan Documents or any related definitions, including, without limitation, the definition of Adjusted Continuing Business EBITDA, which directly restricts the Borrower from making payments under the Subordinated Documents which would otherwise be permitted under the Loan Documents as in effect on the date hereof, (v) extend the final maturity date of the Senior Indebtedness beyond the scheduled maturity date of the Subordinated Notes as in effect on the date hereof, or (x) contravene the provisions of this Agreement. This Agreement shall survive any sale, assignment, disposition or other transfer of all or any portion of the Senior Indebtedness, and the terms of this Agreement shall be binding upon the successors and assigns of the Senior Creditor.

9. Subordinated Creditor Representations. Each Subordinated Creditor hereby represents and warrants to, and covenants and agrees with, the Senior Creditor that as of the date hereof (a) such Subordinated Creditor has not assigned or transferred any of the Subordinated Indebtedness or any interest therein or any guaranties, collateral or other security therefor, if any, to any other person or entity, (b) as of the date hereof the aggregate principal amount at maturity of the Subordinated Notes is \$6,096,996.21, (c) no interest has accrued or been paid on the Subordinated Notes, (d) no Event of Default (as defined in the Subordinated Notes or the other Subordinated Documents or any other agreement, document or instrument evidencing, securing or guaranteeing the payment of or otherwise relating to any of the Subordinated Indebtedness) has occurred and is continuing, (e) it has the requisite power and authority to enter into, execute, deliver, and carry out the terms of this Agreement, (f) this Agreement, when executed and delivered, will constitute the valid and legally binding obligation of such Subordinated Creditor enforceable in accordance with its terms, except as such enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditors' rights generally and by equitable principles and (g) any notes or written obligations

now or hereafter taken to evidence any of the Subordinated Indebtedness (including, without limitation, the Subordinated Notes), and any renewal notes or written obligations, will be endorsed with a legend to the effect that "THIS INSTRUMENT, AND ALL TERMS AND CONDITIONS SET FORTH IN THIS INSTRUMENT AND THE RIGHTS OF THE PARTIES HERETO ARE SUBJECT TO A SUBORDINATION AGREEMENT IN FAVOR OF BANK OF THE WEST."

10. Senior Creditor Representations . The Senior Creditor hereby represents and warrants to, and covenants and agrees with, the Subordinated Creditors that (a) the Senior Creditor has not assigned or transferred any of the Senior Indebtedness or any interest therein or any guaranties, collateral or other security therefor, if any, to any other person or entity, (b) no Default or Event of Default (as such terms are defined in the Senior Note or the other Loan Documents or any other agreement, document or instrument evidencing, securing or guaranteeing the payment of or otherwise relating to any of the Senior Indebtedness) has occurred and is continuing, (c) it has the requisite power and authority to enter into, execute, deliver, and carry out the terms of this Agreement and (d) this Agreement, when executed and delivered, will constitute the valid and legally binding obligation of Senior Creditor enforceable in accordance with its terms, except as such enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditors' rights generally and by equitable principles.

11. Subordinated Creditor Waivers . Each Subordinated Creditor hereby waives notice of acceptance hereof, notice of the creation of any of the Senior Indebtedness pursuant to the terms of the Senior Loan Agreement, the giving or extension of credit to Borrower pursuant to the terms of the Senior Loan Agreement or the taking or releasing of guaranties, collateral or other security for the payment thereof, and hereby waives presentment, demand, protest, or notice of protest.

12. Notice of Default . Each Subordinated Creditor hereby covenants and agrees to give the Senior Creditor prompt written notice of any Event of Default or any default or event of default under or within the meaning of any of the Subordinated Notes or any other agreement, document or instrument evidencing, securing, guaranteeing the payment of or otherwise relating to any of the Subordinated Indebtedness in each case of which such Subordinated Creditor has knowledge at the same time such notice is given to Borrower and to the extent any action or time period hereunder is conditioned upon prior notice to the Senior Creditor of such a default or event of default, such action may not be taken by such Subordinated Creditor (or with respect to a time period, shall not begin to run) until such notice is given to the Senior Creditor.

13. Permitted Actions by Senior Creditor . Each Subordinated Creditor hereby acknowledges and agrees that subject to Paragraph 8(b), the Senior Creditor may take or omit to take any or all actions with respect to the Senior Indebtedness or any Collateral permitted by the Loan Documents and applicable law without affecting the Senior Creditor's rights, or the Subordinated Creditors' rights and obligations, under this Agreement. In particular, but without limitation, the Senior Creditor may, without notice to or consent by the Subordinated Creditors, do any or all of the following:

(a) Alter, compromise, renew, extend, amend, accelerate, or otherwise change any or all of the terms of the Senior Indebtedness, or any part thereof, including increases or decreases in the interest rate thereon;

(b) Take and hold security interests for the payment of the Senior Indebtedness, or exchange, enforce, waive, or release such security interests with or without the substitution of new collateral;

(c) Release, substitute, agree not to sue or deal with Borrower, or sureties, endorsers, or guarantors of the Senior Indebtedness, on any terms or in any manner chosen by the Senior Creditor;

(d) Forbear from or forego pursuing Borrower, or from foreclosing or otherwise realizing upon any security interest or guaranty held by the Senior Creditor in relation to the Senior Indebtedness;

(e) Determine how, when, and what application of payments and credit shall be made with respect to the Senior Indebtedness; or

(f) Assign any or all of the Senior Creditor's rights under this Agreement without notice to or consent by the Subordinated Creditors.

14. No Duty to Share Information . Each Subordinated Creditor hereby assumes responsibility for keeping itself informed of the financial conditions of Borrower and of all other circumstances bearing upon the risk of

nonpayment of the Subordinated Indebtedness that diligent inquiry would reveal, and each Subordinated Creditor hereby agrees that the Senior Creditor shall have no duty to advise such Subordinated Creditor of any information regarding such condition or any such circumstances.

15. Waivers; Remedies Cumulative . Any provision of this Agreement may be amended or waived if, but only if, such amendment or waiver is in a writing signed by the Majority Subordinated Creditors and the Senior Creditor. No failure to exercise, and no delay in exercising on the part of any party hereto, any right, power or privilege under this Agreement shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or privilege under this Agreement preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies provided in this Agreement are cumulative and shall not be exclusive of any rights or remedies provided by law.

16. Notices . Any notice, request, demand, consent, confirmation or other communication under this Agreement shall be in writing and delivered in person or sent by telecopy, recognized overnight courier or registered or certified mail, return receipt requested and postage prepaid, (a) if to the Senior Creditor to Bank of the West, at 222 S.W. Columbia Street, Suite 1200, Portland, Oregon 97201, attention: Sean Edwards, fax number: (503) 223-2915, email: sean.edwards@bankofthewest.com, with copies to Miller Nash LLP, 111 S.W. Fifth Avenue, Suite 3400, Portland, Oregon 97204, attention: Clifton Molatore, fax number: (503) 205-8541, email: clifton.molatore@millernash.com, (b) if to the Subordinated Creditors, to the address set forth on their respective signature pages hereto and (c) with a copy in all cases to Nautilus, Inc., 16400 S.E. Nautilus Drive, Vancouver, Washington 98683, attention: Alec Anderson, email: aanderson@nautilus.com, with a copy to Kirkland & Ellis LLP, 300 N. LaSalle Street, Chicago, Illinois 60602, attention: Jocelyn Hirsch, email: Joeclyn.hirsch@kirkland.com, or to such other address or telecopy number as any such party may designate as its address or telecopy number for communications under this Agreement by notice so given. Such notices shall be deemed effective on the day on which delivered if delivered in person or sent by telecopy, on the first business day after the day on which sent, if sent by recognized overnight courier or on the third business day after the day on which mailed, if sent by registered or certified mail.

17. Further Assurances . Each Subordinated Creditor agrees to do such further acts and things and to execute and deliver such additional agreements, documents, instruments and consents as may be reasonably necessary or as the Senior Creditor may from time to time reasonably request to effect the subordination contemplated by this Agreement.

18. Binding Agreement; Refinancings . This Agreement shall be continuing, irrevocable and binding on the parties hereto, their respective heirs, executors, personal representatives, successors and assigns, and shall inure to the benefit of the parties hereto and their respective successors and assigns. Each Subordinated Creditor further agrees that if Borrower is ever in the process of refinancing all or a portion of the Senior Indebtedness with a new lender, and if the Senior Creditor makes a request of such Subordinated Creditor, such Subordinated Creditor shall agree to enter into a new, substitute subordination agreement with the new lender with terms and conditions substantially similar to the terms and conditions set forth in this Agreement.

19. Severability . In the event any one or more of the provisions contained in this Agreement should be invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions contained herein shall not in any way be affected or impaired thereby.

20. Resurrection of Obligations . This Agreement is of a continuing nature, and it shall continue in force until all the Senior Indebtedness is Paid in Full and the Senior Creditor has no further commitment to lend or otherwise extend credit pursuant to the Senior Loan Agreement and the other Loan Documents. To the extent that the Senior Creditor receives any payment on account of any of the Senior Indebtedness, and any such payment(s) or any part thereof are subsequently invalidated, declared to be fraudulent or preferential, set aside, subordinated and/or required to be repaid to a trustee, receiver or any other person or entity under any bankruptcy act, state or Federal law, common law or equitable cause, then, to the extent of such payment(s) received, the Senior Indebtedness or part thereof intended to be satisfied and any and all subordination obligations and agreements of the Subordinated Creditors hereunder with respect to the Subordinated Indebtedness created and/or existing in favor of the Senior Creditor shall be revived and continue in full force and effect, as if such payment(s) had not been received by the Senior Creditor and applied on account of the Senior Indebtedness. To the extent that the Subordinated Creditors are required to turn over or deliver to the Senior Creditor any amount or property paid or delivered to the Subordinated Creditors under this Paragraph 20, the obligations of Borrower with respect to any such amount or property shall be revived and continued as Subordinated Debt in full force and effect, as if such amount or property had not been paid or received and the Subordinated Creditors shall have the subrogation

rights provided in Paragraph 7.

21. Governing Law . This Agreement shall be governed by and construed in accordance with the substantive laws of the State of Washington (without reference to conflict of law principles).

22. Counterparts . This Agreement may be executed in any number of counterparts (including by facsimile or email transmission), each of which shall be deemed an original and all of which together shall constitute one and the same instrument.

23. No Impairment of Subordinated Indebtedness . The provisions of this Agreement are for the purposes of defining the relative rights of the Senior Creditor, on the one hand, and the Subordinated Creditors, on the other hand. Nothing herein shall impair Borrower's obligations to the Subordinated Creditors to pay principal, interest and other amounts in accordance with the terms of the Subordinated Indebtedness or perform its other obligations thereunder.

24. Headings for Convenience . The Paragraph headings are furnished for the convenience of the parties and are not to be considered in the construction or interpretation of this Agreement.

25. Consent to Jurisdiction; Waiver of Jury Trial . EACH SUBORDINATED CREDITOR HEREBY IRREVOCABLY (a) SUBMITS TO THE NONEXCLUSIVE JURISDICTION OF ANY STATE COURT OR ANY UNITED STATES OF AMERICA COURT SITTING IN KING COUNTY, WASHINGTON, IN ANY SUIT, ACTION OR PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT OR ANY OTHER TRANSACTION DOCUMENT, (b) AGREES THAT ALL CLAIMS IN RESPECT TO SUCH SUIT, ACTION OR PROCEEDING MAY BE HELD AND DETERMINED IN ANY OF SUCH COURTS, (c) WAIVES, TO THE FULLEST EXTENT PERMITTED BY LAW, ANY OBJECTION WHICH SUCH PARTY MAY NOW OR HEREAFTER HAVE TO THE LAYING OF VENUE OF ANY SUCH SUIT, ACTION OR PROCEEDING BROUGHT IN ANY SUCH COURT, (d) WAIVES ANY CLAIM THAT SUCH SUIT, ACTION OR PROCEEDING BROUGHT IN ANY SUCH COURT HAS BEEN BROUGHT IN AN INCONVENIENT FORUM AND (e) WAIVES ALL RIGHTS OF ANY OTHER JURISDICTION WHICH SUCH PARTY MAY NOW OR HEREAFTER HAVE BY REASON OF ITS PRESENT OR SUBSEQUENT DOMICILES. EACH SUBORDINATED CREDITOR AUTHORIZES THE SERVICE OF PROCESS UPON SUCH PARTY BY REGISTERED MAIL SENT TO SUCH PARTY AT ITS ADDRESS REFERENCED IN PARAGRAPH 16 ABOVE. THE SUBORDINATED CREDITORS AND THE SENIOR CREDITOR HEREBY IRREVOCABLY WAIVE THE RIGHT TO TRIAL BY JURY WITH RESPECT TO ANY ACTION IN WHICH THE SUBORDINATED CREDITORS AND THE SENIOR CREDITOR ARE PARTIES RELATING TO OR ARISING OUT OF OR IN CONNECTION WITH THIS AGREEMENT OR THE SENIOR NOTE OR SUBORDINATED NOTE.

26. Termination . This Agreement shall continue in full force and effect until the Senior Indebtedness is Paid in Full and the Senior Creditor has no further commitments to lend or otherwise extend credit pursuant to the Senior Loan Agreement or any other Loan Document.

[Remainder of page intentionally blank.]

EXECUTION COPY

IN WITNESS WHEREOF, the undersigned have executed this Subordination Agreement as of September 3, 2010.

SENIOR CREDITOR:

BANK OF THE WEST

By: /s/ Sean Edwards

Sean Edwards, Vice President

[Signature Page to Subordination Agreement]

SUBORDINATED CREDITORS:

SHERBORNE STRATEGIC FUND A, LLC

By: /s/ Craig L. McKibben

Name: Craig L. McKibben

Title: Managing Director

**Sherborne Investors LP as Managing
Member**

Address: c/o Sherborne Investors LP

135 East 57th Street

New York, NY 10022

[Signature Page to Subordination Agreement]

SHERBORNE STRATEGIC FUND B, LLC

By: /s/ Craig L. McKibben
Name: ;- Craig L. McKibben
Title: Managing
Director,
Sherborne Investors LP as Managing Member

Address: c/o Sherborne Investors
LP
135 East 57th Street
New York, NY 10022

[Signature Page to Subordination Agreement]

NOTTINGHAM INVESTORS LLC

By: /s/ Craig L. McKibben
Name: Craig L. McKibben
Title: Managing Director,
Sherborne Investors LP as Managing
Member

Address: c/o Sherborne Investors LP
135 East 57th Street
New York, NY 10022

[Signature Page to Subordination Agreement]

EXECUTION COPY

Borrower hereby assents to the foregoing Subordination Agreement and agrees in all respects to be bound thereby. Borrower agrees (i) not to make any payment of any principal, interest or other amounts on or with respect to any of the Subordinated Indebtedness in violation of the terms and conditions of the foregoing Subordination Agreement, (ii) not to amend, change, modify or supplement the Subordinated Notes or the other Subordinated Documents in violation of this Agreement without the prior written consent of the Senior Creditor and (iii) not to amend, change, modify or supplement the Senior Notes, the Senior Loan Agreement or the other Loan Documents in violation of this Agreement without the prior written consent of the Majority Subordinated Creditors. Borrower agrees that the Subordinated Creditors shall not be prohibited from taking any action at any time that is required under applicable law to toll any applicable statute of limitations that would otherwise prevent the Subordinated Creditors from preserving any claim with respect to the Subordinated Indebtedness, provided that the Subordinated Creditors simultaneously provides the Senior Creditor with written notice thereof.

Executed as of September 3, 2010.

/s/ Kenneth Fish

BORROWER:

NAUTILUS, INC.

By:

Name: Kenneth Fish

Title: Chief Financial Officer

[Signature Page to Subordination Agreement]

CERTIFICATION

I, Edward J. Bramson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Nautilus, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

< div style="line-height:120%;padding-top:5px;padding-left:36px;text-align:left;text-indent:-36px;font-size:10pt;">5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting,

November 8, 2010

Date

By: /s/ Edward J. Bramson

< font style="font-family:inherit;font-size:10pt;">Edward J.

Bramson

Chairman and Chief Executive Officer

(Principal Executive Officer)

CERTIFICATION

I, Kenneth L. Fish, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Nautilus, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 8, 2010

Date

By: /s/ Kenneth L. Fish

Kenneth L. Fish

Chief Financial Officer

(Principal Financial Officer)

Certification

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Nautilus, Inc., a Washington corporation (the "Company"), does hereby certify that:

To my knowledge, the Quarterly Report on Form 10-Q for the period ended September 30, 2010 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 8, 2010

Date

By: /s/ Edward J. Bramson

Edward J. Bramson

Chairman and Chief Executive Officer

(Principal Executive Officer)

To my knowledge, the Quarterly Report on Form 10-Q for the period ended September 30, 2010 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

November 8, 2010

Date

By: /s/ Kenneth L. Fish

Kenneth L. Fish

Chief Financial Officer

(Principal Financial Officer)