JOE'S JEANS INC.
Form 10-Q
October 13, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended August 31, 2015

OR

o 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: 0-18926

JOE S JEANS INC.

(Exact name of registrant as specified in its charter)

Delaware	**11-2928178**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2340 South Eastern Avenue, Commerce, California	**90040**
(Address of principal executive offices)	(Zip Code)

(323) 837-3700

(Registrant s telephone number, including area code)

NO CHANGE

(Former name, former address and former fiscal year, if changed since last report)

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. x Yes o No

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

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

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

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

The number of shares of the registrant s common stock outstanding as of October 13, 2015 was 69,968,208.

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JOE S JEANS INC.

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PART I FINANCIAL INFORMATION

Item 1. **Financial Statements.**

JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

	August 31, 2015 (unaudited)		November 30, 2014 (unaudited)	
ASSETS				
Current assets				
Cash and cash equivalents	$	368	$	1,054
Accounts receivable, net		142		1,279
Factored accounts receivable, net		8,518		11,105
Inventories, net		15,350		25,354
Deferred income taxes, net		5,786		6,065
Prepaid expenses and other current assets		1,512		1,212
Current portion of assets held for sale		72,532		57,050
Total current assets		104,208		103,119
Property and equipment, net		1,832		2,897
Goodwill		8,394		8,394
Intangible assets		55,022		56,773
Deferred financing costs		1,295		1,611
Other assets		778		881
Assets held for sale, net of current portion				30,274
Total assets	$	171,529	$	203,949
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities				
Accounts payable and accrued expenses	$	13,797	$	12,477
Buy-out payable		3,277		3,277
Line of credit		19,587		31,338
Short-term debt		59,183		59,003
Current portion of liabilities held for sale		4,623		10,854
Total current liabilities		100,467		116,949
Convertible notes		26,762		24,733
Deferred income taxes, net		18,373		17,765
Deferred rent		2,981		2,830
Other liabilities		393		643
Long-term liabilities held for sale				32
Total liabilities		148,976		162,952

Commitments and contingencies				
Stockholders equity				
Common stock, $0.10 par value: 100,000 shares authorized, 70,802 shares issued and 69,968 outstanding (2015) and 69,822 shares issued and 69,298 outstanding (2014)		7,082		6,984
Additional paid-in capital		111,870		111,010
Accumulated deficit		(92,964)		(73,679)
Treasury stock, 834 shares (2015), 524 shares (2014)		(3,435)		(3,318)
Total stockholders equity		22,553		40,997
Total liabilities and stockholders equity	$	171,529	$	203,949

See accompanying notes to condensed consolidated financial statements.

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JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF NET LOSS AND COMPREHENSIVE LOSS

(in thousands, except per share data)

	Three months ended		Nine months ended	
	August 31, 2015	August 31, 2014	August 31, 2015	August 31, 2014
	(unaudited)		(unaudited)	
Net sales	$ 18,865	$ 25,718	$ 61,266	$ 68,957
Cost of goods sold	10,542	13,279	35,190	36,301
Gross profit	8,323	12,439	26,076	32,656
Operating expenses				
Selling, general and administrative	11,443	10,585	34,895	31,220
Depreciation and amortization	799	905	2,448	2,728
Retail stores impairment	470	332	470	332
	12,712	11,822	37,813	34,280
Operating income (loss)	(4,389)	617	(11,737)	(1,624)
Other income				(2,268)
Interest expense	1,700	1,279	4,637	3,796
Income (loss) from continuing operations, before provision for income taxes	(6,089)	(662)	(16,374)	(3,152)
Income tax expense (benefit)	(12,801)	(174)	1,698	(860)
Income (loss) from continuing operations	6,712	(488)	(18,072)	(2,292)
Income (loss) from discontinued operations, net of tax	(1,053)	764	(1,213)	2,729
Net income (loss) and comprehensive income (loss)	$ 5,659	$ 276	$ (19,285)	$ 437
Earnings (loss) per common share - basic				
Earnings (loss) from continuing operations	0.10	(0.01)	(0.26)	(0.03)
Earnings (loss) from discontinued operations	(0.02)	0.01	(0.02)	0.04
Earnings (loss) per common share - basic	$ 0.08	$ 0.00	$ (0.28)	$ 0.01
Earnings (loss) per common share - diluted				
Earnings (loss) from continuing operations	$ 0.10	$ (0.01)	$ (0.26)	$ (0.03)
Earnings (loss) from discontinued operations	(0.02)	0.01	(0.02)	0.04
Earnings (loss) per common share - diluted	$ 0.08	$ 0.00	$ (0.28)	$ 0.01
Weighted average shares outstanding				
Basic	69,614	68,362	69,314	68,151
Diluted	69,620	68,880	69,314	68,935

See accompanying notes to condensed consolidated financial statements.

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JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Nine months ended	
	August 31, 2015	August 31, 2014
	(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net cash (used in) provided by continuing operations	$ 4,036	$ (2,793)
Net cash (used in) provided by discontinued operations	7,665	(3,652)
Net cash (used in) provided by operating activities	11,701	(6,445)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(102)	(95)
Business acquisition		(418)
Net cash used in continuing investing activities	(102)	(513)
Net cash used in discontinued investing activities	(349)	(470)
Net cash used in investing activities	(451)	(983)
CASH FLOWS FROM FINANCING ACTIVITIES		
(Repayment of) proceeds from line of credit	(4,435)	5,365
Payments of promissory note		(1,235)
Repayment of term loan		(75)
Payment of taxes on restricted stock units	(68)	(343)
Purchase of restricted stock	(117)	(227)
Net cash (used in) provided by continuing financing activities	(4,620)	3,485
Cash (used in) provided by discontinued financing activities	(7,316)	4,122
Net cash (used in) provided by financing activities	(11,936)	7,607
NET CHANGE IN CASH AND CASH EQUIVALENTS	(686)	179
CASH AND CASH EQUIVALENTS, at beginning of period	1,054	785
CASH AND CASH EQUIVALENTS, at end of period	$ 368	$ 964

See accompanying notes to condensed consolidated financial statements.

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JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(in thousands)

	Common Stock		Additional	Accumulated	Treasury	Total Stockholders
	Shares	Par Value	Paid-In Capital	Deficit	Stock	Equity
Balance, November 30, 2013	68,878	$ 6,890	$ 107,933	$ (45,963)	$ (3,091)	$ 65,769
Net income and comprehensive income (unaudited)				437		437
Embedded conversion feature net of taxes (unaudited)			2,058			2,058
Stock repurchase (unaudited)					(227)	(227)
Stock-based compensation, net of withholding taxes (unaudited)			595			595
Issuance of restricted stock (unaudited)	889	89	(89)			
Balance, August 31, 2014 (unaudited)	69,767	$ 6,979	$ 110,497	$ (45,526)	$ (3,318)	$ 68,632
Balance, November 30, 2014	69,822	$ 6,984	$ 111,010	$ (73,679)	$ (3,318)	$ 40,997
Net income and comprehensive income (unaudited)				(19,285)		(19,285)
Embedded conversion feature net of taxes (unaudited)						
Stock repurchase (unaudited)					(117)	(117)
Stock-based compensation, net of withholding taxes (unaudited)			958			958
Issuance of restricted stock (unaudited)	980	98	(98)			
Balance, August 31, 2015 (unaudited)	70,802	$ 7,082	$ 111,870	$ (92,964)	$ (3,435)	$ 22,553

See accompanying notes to condensed consolidated financial statements.

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JOE S JEANS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 BASIS OF PRESENTATION

Our principal business activity involves the design, development and worldwide marketing of apparel products, which include denim jeans, related casual wear and accessories that bear the brand Joe s® and Hudson®. Our primary current operating subsidiaries are Joe s Jeans Subsidiary, Inc. (***Joe s Jeans Subsidiary***) and Hudson Clothing, LLC (***Hudson***). In addition, we have other subsidiaries, including Joe s Jeans Retail Subsidiary, Inc., Innovo West Sales, Inc., Hudson Clothing Holdings, Inc. and HC Acquisition Holding, Inc. All significant inter-company transactions have been eliminated. We completed the acquisition of Hudson on September 30, 2013 and the information presented includes the results of operations of Hudson from the date of acquisition. On September 11, 2015, we completed the sale of certain of our operating and intellectual property assets related to the Joe s® brand and business to two separate purchasers for an aggregate purchase price of $80 million, the proceeds of which were used to repay all of our indebtedness outstanding under our term loan credit agreement with Garrison Loan Agency Service LLC and a portion of our indebtedness outstanding under our revolving credit agreement with CIT Commercial Services, Inc., a unit of CIT Group. See Note 2 Subsequent Events for additional information related to this and other transactions. As a result, we reported the operating results of our Joe s business in Income (loss) from discontinued operations, net of tax in our condensed consolidated statements of net loss and comprehensive loss for all periods presented. In addition, the assets and liabilities associated with our Joe s business are reported as held for sale (discontinued operations), in the condensed consolidated balance sheets for all periods presented. (see Note 3 Discontinued Operations). Unless otherwise indicated, the disclosures accompanying the condensed consolidated financial statements reflect our continuing operations.

Our reportable business segments are Wholesale and Retail. We manage, evaluate and aggregate our operating segments for segment reporting purposes primarily on the basis of business activity and operation. Our Wholesale segment is comprised of sales of Hudson® products to retailers, specialty stores and international distributors, includes revenue from licensing agreements and records expenses from sales, trade shows, distribution, product samples and customer service departments. Our Retail segment is comprised of sales to consumers through ten of our Joe s branded full price retail stores, 11 outlet stores and through our online retail site at *www.hudsonjeans.com*. Our Corporate and other is comprised of expenses from corporate operations, which include the executive, finance, legal, human resources, design and production departments and general advertising expenses associated with our brands. Sales of our Joe s® products are reported as discontinued operations.

Our unaudited condensed consolidated financial statements, which include the accounts of our wholly-owned subsidiaries, for the three and nine months ended August 31, 2015 and 2014 and the related footnote information have been prepared on a basis consistent with our audited consolidated financial statements as of November 30, 2014 contained in our Annual Report on Form 10-K for the fiscal year ended November 30, 2014, or the Annual Report. Our fiscal year end is November 30. Each fiscal year, as presented, is 52 weeks.

Going Concern

The accompanying consolidated financial statements for the year ended November 30, 2014 and three and nine months ended August 31, 2015 were prepared under the assumption that we will continue to operate as a going concern, which contemplates the realization of assets and the liquidation of liabilities in the ordinary course of business. We face various uncertainties that raise substantial doubt about our ability to continue as a going concern. These financial statements do not include any adjustments that may result from the outcome of these uncertainties.

On November 6, 2014, we received an initial notice of default and event of default and demand for payment of default interest under the term loan credit facility for violating certain financial and maintenance covenants from Garrison Loan Agency Service LLC (***Garrison***). As of August 31, 2015, we were not in compliance with certain financial and maintenance covenants under the term loan credit agreement. As a result of the events of default under the term loan credit agreement, this also triggered a default and an event of default under the terms of the revolving credit agreement with CIT Commercial Services, Inc., a unit of CIT Group, (***CIT***). Both lenders reserved their respective rights to exercise any and all remedies available to them under their respective agreements and demanded payment of interest under those agreements at the default rate of interest. In addition, as a result of the events of default under the term loan credit agreement and the revolving credit agreement, we also were in default of our subordinated convertible notes issued to the former equity owners of Hudson. Under the terms of the revolving credit and term loan credit agreements, we were prohibited from

making any payments under the subordinated convertible notes, but we were accruing interest on the convertible notes at the default rate. We were also prohibited from making earn-out payments to our former creative director, Mr. Dahan under his buy-out agreement.

On September 11, 2015, our indebtedness outstanding under the term loan credit agreement was fully repaid with a portion of the proceeds of the sale of certain Joe s assets. As a result, the term loan credit agreement was paid in full and terminated on September 11, 2015. We also used a portion of the proceeds from the asset sale to repay a substantial portion of our indebtedness under the revolving credit agreement, and on September 11, 2015, we entered into an amended and restated revolving credit agreement, which waived our existing defaults, forbearance defaults and certain other defaults. See Note 2 Subsequent Events for a further discussion of the asset sales, the repayment of certain obligations under our agreements with Garrison and CIT, and the terms of our amended and restated revolving credit agreement.

NOTE 2 SUBSEQUENT EVENTS

On September 8, 2015, we entered into the definitive agreements described below (collectively, the ***Transaction Agreements***) in which, subject to the completion of the conditions described below, we (i) sold certain of our operating and intellectual property assets related to the Joe s Business to two separate purchasers for an aggregate purchase price of $80 million (the ***Asset Sale***), the proceeds of which were used to repay all of our indebtedness outstanding under our term loan credit agreement with Garrison Loan Agency Service LLC and a portion of our indebtedness outstanding under our revolving credit agreement with CIT Commercial Services, Inc. (***CIT***), a unit of CIT Group; (ii) will combine our remaining business operated under the Hudson® brand with RG Parent, LLC, a Delaware limited liability company (***RG*** or ***Robert Graham***), pursuant to the Merger Agreement (defined below), (iii) will issue and sell $50 million of a new series of the Company s preferred stock in a private placement to an affiliate of Tengram Capital Partners, L.P. (***TCP***); and (iv) will exchange outstanding convertible notes for a combination of cash, shares of our common stock, $0.10 par value per share (***Common Stock***), and modified convertible notes (the ***Modified Convertible Notes***) (collectively, the ***Merger Transactions***). RG is a portfolio company of TCP and its principal business activity involves the design, development and marketing of luxury lifestyle brand apparel products under the brand Robert Graham®.

After the completion of the Asset Sale, we expect to change our name to Differential Brands Group Inc. After the completion of the Merger and the Merger Transactions, the RG equity holders will own approximately 44.8% of our Common Stock, the preferred stock owned by TCP will be convertible into approximately 22.8% of our Common Stock, the convertible noteholders will own approximately 18.2% of our Common Stock and the existing stockholders (including the outstanding equity awards under our incentive plan) will own approximately 13.5% of our Common Stock, all on a fully diluted basis, assuming the modified convertible notes are converted and calculated at the market price on September 30, 2015. In connection with the Merger and the Merger Transactions, we expect that we will enter into new financing arrangements pursuant to which we will have approximately $25 million of indebtedness outstanding under a new revolving credit facility and $50 million of indebtedness outstanding under a new term loan credit facility, the proceeds of which will be used to repay our remaining indebtedness outstanding under the revolving credit agreement with CIT and certain indebtedness owed to the holders of the convertible notes and Joseph M. Dahan. See Risk Factors for an additional discussion regarding the risks and uncertainties related to the Merger and Merger Transactions.

IP Asset Purchase Agreement

On September 8, 2015, we, along with Joe s Holdings LLC, a Delaware limited liability company (***IP Assets Purchaser***), and solely for the purposes of its related guarantee, Sequential Brands Group, Inc., a Delaware corporation , entered into an asset purchase agreement (the ***IP Asset Purchase Agreement***), pursuant to which, the IP Assets Purchaser, among other things, purchased certain intellectual property assets (the ***Intellectual Property Assets***) used or held for use in our business operated under the brand names Joe s Jeans, Joe s, Joe s JD and else (the ***Business***). The aggregate purchase price was $67 million. Additionally, at the closing of the sale, the IP Assets Purchaser deposited $2.5 million to an escrow account, which will be used to defer certain costs and expenses which may be incurred by us after the closing of the transaction.

The IP Asset Purchase Agreement contains representations and warranties, covenants related to our operations and business, and indemnification rights of both parties after the closing of the transaction that are customary for transactions of this type.

We will retain and operate the 32 Joe s® brand retail stores after the closing of the Operating Asset Purchase Agreement and the IP Asset Purchase Agreement and thereafter will proceed with the disposition of certain stores; provided, however that, certain retail stores designated by Operating Assets Purchaser will be transferred to the Operating Assets Purchaser on or prior to December 31, 2016 for no additional consideration. Subject to certain limitations on our aggregate net liability with respect to the net costs and expenses related to the operation of the retail stores if the Merger Transactions do not close, such costs and expenses will be borne by us, the IP Assets Purchaser and the Operating Assets Purchaser. The Operating Assets Purchaser will supply Joe s® branded merchandise to the retail stores for resale under a license from the IP Assets Purchaser.

Operating Asset Purchase Agreement

On September 8, 2015, we, along with GBG USA Inc., a Delaware corporation (***Operating Assets Purchaser***), entered into an asset purchase agreement (the ***Operating Asset Purchase Agreement*** and together with the IP Asset Purchase Agreement, the ***Asset Purchase Agreements***), pursuant to which, the Operating Assets Purchaser, among other things, purchased certain inventory and other assets and assume certain liabilities from us and our subsidiaries related to the Joe s Business, including certain employees of the Joe s Business and at a later date, specified Joe s store leases. The aggregate purchase price was $13 million. Additionally, at the closing of the sale, the Operating Assets Purchaser deposited $1.5 million into an escrow account, which will be used to defer certain costs and expenses which may be incurred by the Company

after the closing of the transaction.

The Operating Asset Purchase Agreement contains representations and warranties, covenants of the Company, and indemnification rights of both parties after the closing of the transaction that are customary for transactions of this type.

On September 11, 2015, we completed the Asset Sale of the Joe s Business pursuant to the respective Asset Purchase Agreements. The proceeds were used to repay all of our indebtedness outstanding under the term loan credit agreement and a portion of our indebtedness outstanding under our revolving credit agreement.

Agreement and Plan of Merger

On September 8, 2015, we entered into an Agreement and Plan of Merger (the ***Merger Agreement***) with JJ Merger Sub LLC, a Delaware limited liability company and our wholly owned subsidiary (***Merger Sub***), and RG, pursuant to which Merger Sub will merge with and into RG on the terms and subject to the conditions set forth in the Merger Agreement (the ***Merger***), with RG surviving the Merger as our wholly-owned subsidiary. Subject to the conditions set forth in the Merger Agreement, the Merger is expected to close in the fourth quarter of 2015.

At the effective time of the Merger (the ***Effective Time***), on the terms and subject to the conditions set forth in the Merger Agreement, all of the common units of RG (the ***RG Units***) outstanding immediately prior to the Effective Time will be converted into the right to receive an aggregate of $81 million in cash (the ***Aggregate Cash Consideration***) and 8,870,968 shares of Common Stock (after giving effect to a 1 for 30 reverse stock split) (the ***Aggregate Stock Consideration*** and, together with the Aggregate Cash Consideration, the ***Aggregate Merger Consideration***). The portion of the Aggregate Merger Consideration constituting the Aggregate Cash Consideration will be reduced by an amount necessary to satisfy certain indebtedness of RG outstanding as of the Effective Time (as adjusted, the ***Actual Cash Consideration*** and, together with the Aggregate Stock Consideration, the ***Actual Merger Consideration***).

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The Merger Agreement contains customary representations, warranties and covenants of us and RG.

The completion of the Merger is subject to customary closing conditions, including, among others, (i) our stockholder approval of: (x) the issuance of Common Stock in connection with the Merger, (y) the issuance of Common Stock upon conversion of the Company s Series A Preferred Stock (defined below) pursuant to the Stock Purchase Agreement (as defined below), and (z) a charter amendment to effect a 1 for 30 reverse stock split of our Common Stock (the ***Reverse Stock Split***), (ii) consummation of the asset sales pursuant to each of the IP Asset Purchase Agreement and Operating Asset Purchase Agreement, (iii) consummation of the transactions contemplated by the Stock Purchase Agreement (defined below), (iv) consummation of the transactions contemplated by the Rollover Agreement (as defined below), (v) RG must have obtained financing or the persons who have committed to provide financing must be prepared to provide the financing immediately following the Effective Time, (vi) the Registration Statement on Form S-4 registering the Common Stock to be issued in connection with the Merger must have become effective, (vii) the Common Stock to be issued in the Merger must be authorized for listing on NASDAQ and (viii) since the date of the Merger Agreement, there must not be any changes, events, effects, developments, occurrences or state of facts that, individually or in the aggregate would reasonably be expected to have a material adverse effect on us or RG, subject to customary exceptions.

The Merger Agreement may be terminated under certain circumstances, including if the Merger has not been consummated on or before February 8, 2016.

We have agreed to pay RG a termination fee of $5.25 million, less certain expenses, if: (i) we terminate the Merger Agreement under certain circumstances and within twelve months after such termination, consummates a takeover proposal or enters into a definitive agreement with respect to a takeover proposal; (ii) the Merger Agreement is terminated by RG as a result of the Board changing its recommendation with respect to the Merger and related transactions; or (iii) the Merger Agreement is terminated by us because we have received a superior proposal and enter into a definitive agreement with respect thereto. In the event that the Merger Agreement is terminated by us because of RG s failure to obtain financing or by RG because the Merger has not occurred by February 8, 2016 at a time that we would have the right to terminate pursuant to a financing issue and have provided notice of such right, in each case, so long as we are not in breach of certain obligations related to obtaining the financing, then RG must pay us a reverse termination fee of $7.5 million, less certain expenses they may have been previously reimbursed to us. If either party terminates the Merger Agreement as a result of the other party s breach, then the breaching party must pay the non-breaching party up to an aggregate amount of $3 million for all of the documented out-of-pocket fees and expenses incurred in connection with the Merger Agreement and related transactions.

Stock Purchase Agreement

On September 8, 2015, we entered into a stock purchase agreement (the ***Stock Purchase Agreement***) with TCP Denim, LLC, a Delaware limited liability company and affiliate of TCP (the ***Purchaser***), pursuant to which we will issue and sell to Purchaser immediately prior to the consummation of the Merger an aggregate of fifty thousand (50,000) shares of the Company s preferred stock, par value $0.10 per share, designated as Series A Convertible Preferred Stock (the ***Series A Preferred Stock***), for an aggregate purchase price of $50 million in cash. Concurrently with the execution of the Stock Purchase Agreement, Tengram Capital Partners Fund II, L.P., a Delaware limited partnership, is entering into a limited guaranty in favor of us with respect to the obligations of the Purchaser under the Stock Purchase Agreement to pay the purchase price.

The Stock Purchase Agreement also provides that the proceeds from the sale of Series A Preferred Stock must be used for the purposes of consummating the Merger and the transactions contemplated by the Merger Agreement. The Stock Purchase Agreement provides that at the Effective Time, the applicable number of directors on our Board will resign such that only two directors on the Board immediately prior to the

closing will remain on the Board immediately following the closing. Furthermore, as of the Effective Time, the Board shall appoint the three persons designated by Purchaser to fill three of such vacancies as a director. A remaining vacancy will be filled by our chief executive officer following the Effective Time.

The following is a summary of the terms of the Series A Preferred Stock as set forth in the form of certificate of designation for the Series A Preferred Stock: (i) each share of Series A Preferred Stock entitles the holder thereof to receive cumulative cash dividends, payable quarterly, at an annual rate of 10%, plus accumulated and accrued dividends thereon through such date; additionally, if the Board declares or pays a dividend on the Common Stock, then each holder of the Series A Preferred Stock will be entitled to receive a cash dividend on an as converted basis; (ii) each holder of the Series A Preferred Stock is entitled to vote on an as converted basis and together with the holders of Common Stock as a single class, subject to certain limitations; (iii) for so long as a to be determined percent of the shares of the Series A Preferred Stock remain outstanding, the holders of the Series A Preferred Stock,

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exclusively and as a separate class, will be entitled to elect three (3) members of the Board (the ***Series A Directors***), and such Series A Director may only be removed without cause by the affirmative vote of the holders of a majority of the shares of Series A Preferred Stock; (iv) the holders of the Series A Preferred Stock have separate class voting rights with respects to certain matters affecting their rights; (v) upon any liquidation event, holders of the Series A Preferred Stock are entitled to receive the greater of the liquidation preference on the date of determination and the amount that would be payable to the holders of the Series A Preferred Stock had such holders converted their shares of Series A Preferred Stock into shares of Common Stock immediately prior to such liquidation event; and (vi) each share of the Series A Preferred Stock is convertible, at the option of the holder thereof, at any time and without the payment of additional consideration by the holder, at an initial conversion price of $11.10 (after taking into account the 1 for 30 reverse stock split).

Rollover Agreement

On September 8, 2015, we entered into a rollover agreement (the ***Rollover Agreement***) with the holders of convertible notes (the ***Convertible Notes***), pursuant to which they have agreed to contribute to us the Convertible Notes in exchange for the following:

- issuance of a number of shares of our Common Stock with a value per share of $11.10 equal to the sum (i) of a specified percentage of the principal amount of Convertible Notes held by such noteholder, which principal amount, as of July 1, 2015, is an aggregate of $33,990,538 and will be increased by any PIK interest payable in accordance with the terms of the Convertible Notes until the time that is immediately prior to the Effective Time (the ***Rollover Time***), and (without duplication) and (ii) all accrued interest, including default interest as applicable, owing on 50% of the principal amount of such Convertible Notes in accordance with the terms of the Convertible Notes as of the Rollover Time, which amount, as of July 1, 2015, is an aggregate of $1,936,617 and which will continue to accrue interest in accordance with the terms of the Convertible Notes until the Rollover Time. The holders of Convertible Notes will receive in the aggregate approximately 14.0% of our Common Stock outstanding immediately after consummation of the Merger;

- a cash payment to each noteholder equal to twenty-five percent (25%) of the principal amount of Convertible Notes as of the Rollover Time held by each such holder of the Convertible Notes, which principal amount, as of July 1, 2015, is an aggregate of $33,990,538, which will be increased by any PIK interest payable in accordance with the terms of the Convertible Notes until the Rollover Time; and

- Modified Convertible Notes with a principal amount equal to the sum of (i) a specified percentage of the principal amount of Convertible Notes as of the Rollover Time held by each holder of the Convertible Notes, which principal amount, as of July 1, 2015, is an aggregate of $33,990,538 and will be increased by any PIK interest payable in accordance with the terms of the Convertible Notes until the Rollover Time, and (without duplication) (ii) all accrued interest, including default interest as applicable, owing on 50% of the principal amount of the Convertible Notes in accordance with the terms of the Convertible Notes as of the Rollover Time, which amount, as of July 1, 2015, is an aggregate of $1,936,617 and which will continue to accrue interest in accordance with the terms of the Convertible Notes until the Rollover Time. The holders of Convertible Notes will receive in the aggregate approximately $16.4 million outstanding principal amount of Modified Convertible Notes.

The Rollover Agreement will be automatically terminated upon termination of the Merger Agreement prior to the Rollover Time. The Rollover Agreement may also be terminated by us or by Mr. Kim and Fireman Capital CPF Hudson Co-Invest LP (***Fireman***) if the Rollover Time has not occurred prior to April 8, 2016.

The Modified Convertible Notes are structurally and contractually subordinated to our senior debt and will mature five and a half years following the date of such note. The Modified Convertible Notes accrue interest quarterly on the outstanding principal amount at a rate of 6.5% per annum (to be increased to 7% as of October 1, 2016 with respect to the Modified Convertible Notes issued to Fireman), which will be payable 50% in cash and 50% in additional paid in kind (***PIK Notes***); provided, however, that we may, in our sole discretion, elect to pay 100% of such interest in cash. Beginning upon the date of issuance, the Modified Convertible Notes will be convertible by each of the holders into shares of Common Stock, cash, or a combination of cash and Common Stock, at our election.

If we elect to issue only shares of Common Stock upon conversion of the Modified Convertible Notes, each of the Modified Convertible Notes would be convertible, in whole but not in part, into a number of shares equal to the conversion amount divided by the market price. The conversion amount is (a) the product of (i) the market price, multiplied by (ii) the quotient of (A) the principal amount, divided by (B) the conversion price, minus (b) the aggregate optional prepayment amounts paid to the holder. The market price is the average of the closing prices for the Common Stock over the 20 trading day period immediately preceding the notice of conversion. If we elect to pay cash with respect to a conversion of the Modified Convertible Notes, the amount of cash to be paid per share will be equal to the conversion amount. We will have the right to prepay all or any portion of the principal amount of the Modified Convertible Notes at any time so long as it makes a pro rata prepayment on all of the Modified Convertible Notes.

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Registration Rights Agreement

At the Effective Time, we expect to enter into a registration rights agreement (the ***Registration Rights Agreement***) with the Purchaser under the Stock Purchase Agreement and the holders of the Convertible Notes party to the Rollover Agreement. Pursuant to the Registration Rights Agreement, we will provide certain demand registration rights to register the shares of Common Stock issued in connection with the Rollover Agreement, and issuable upon conversion of the Modified Convertible Notes and Series A Preferred Stock, on registration statements on Form S-1 or Form S-3, subject to certain limitations as described therein, and will also provide certain piggy back registration rights.

Voting Agreement

On September 8, 2015, we entered into a voting agreement, with RG and Joseph M. Dahan, our Creative Director and Director, pursuant to which Mr. Dahan has agreed to vote all of the Common Stock he holds in a manner so as to facilitate consummation of the Merger. As of the date hereof, Mr. Dahan owns approximately 17% of our outstanding voting stock.

CIT Agreements

On September 11, 2015, we entered into (i) the A&R Revolving Credit Agreement (as defined below), (ii) the Reaffirmation and Amendment of Collateral Documents (as defined below), and (iii) the Reassignment and Termination Agreement (as defined below).

A portion of the proceeds of the Asset Sale (as defined below) were used to repay all of our indebtedness outstanding under the Term Loan Credit Agreement, dated September 30, 2013 (the ***Term Loan Credit Agreement***), with Garrison Loan Agency Services LLC (***Garrison***), as administrative agent, collateral agent, lead arranger, documentation agent and syndication agent, and the lenders party thereto. As a result, the Term Loan Credit Agreement was paid in full and terminated on September 11, 2015.

In connection with the Asset Sale, on September 11, 2015, we, along with Hudson Clothing, LLC, our wholly-owned subsidiary (***Hudson*** or the ***Borrower***), as Administrative Borrower, and certain of our other subsidiaries party thereto, as Guarantors, entered into the Amended and Restated Revolving Credit Agreement (the ***A&R Revolving Credit Agreement***) with CIT, as administrative agent and collateral agent , and the lenders party thereto. Among other things, the A&R Revolving Credit Agreement (i) amends and restates the Revolving Credit Agreement, dated as of September 30, 2013 (as amended by (a) Omnibus Amendment No. 1 to Revolving Credit Agreement and Guarantee and Collateral Agreement, dated as of December 20, 2013, (b) Amendment No. 2 to Revolving Credit Agreement, dated as of April 23, 2015, and (c) the CIT Forbearance Agreement (as defined below), by and among Hudson and Joe s Jeans Subsidiary Inc., as borrowers, us and certain of our other subsidiaries as a party thereto, as guarantors, CIT, and the lenders party thereto, and (ii) waives the Existing Defaults and Forbearance Defaults (each as defined under the Forbearance and Amendment No. 3 to Revolving Credit Agreement, dated June 26, 2015, between the Company and CIT (the ***CIT Forbearance Agreement***)) and certain other defaults. Pursuant to a separate consent and agreement, CIT and the lenders consented to the Asset Sale.

The A&R Revolving Credit Agreement provides for a revolving credit facility (the ***Revolving Facility***) with up to $10,000,000 of lender commitments (the ***Revolving Commitment***). The Borrowers actual maximum credit availability under the Revolving Facility varies from time to time and is equal to the lesser of (i) the Revolving Commitment minus an availability block of $2.5 million, or $7.5 million, and (ii) a calculated borrowing base, which is based on the value of the eligible accounts and eligible inventory minus the availability block of $2.5 million minus reserves imposed by the revolving lenders, all as specified in the A&R Revolving Credit Agreement. The Revolving Facility provides for swingline loans, up to $1 million sublimit, and letters of credit, up to $1 million sublimit, within such credit availability limits. Proceeds from advances under the Revolving Facility may be used (i) to pay fees and expenses in connection with the A&R Revolving Credit Agreement and the Asset Sale and (ii) for working capital needs and general corporate purposes.

All unpaid loans under the Revolving Facility mature on December 31, 2015. The Borrowers have the right at any time and from time to time to (i) terminate the commitments under the Revolving Facility in full and (ii) prepay any borrowings under the Revolving Facility, in whole or in part, without terminating or reducing the commitment under the Revolving Facility.

The Revolving Facility is guaranteed by us and all of our subsidiaries, and is secured by liens on substantially all assets owned by the borrowers and guarantors party thereto, subject to permitted liens and exceptions. In connection with the Asset Sale, the Guarantee and Collateral Agreement, dated as of September 30, 2013, by and among Joe s Jeans Subsidiary, Inc. (***Joe s Jeans Subsidiary***). and Hudson, us and certain of our subsidiaries as a party thereto and CIT, as administrative agent and collateral agent, as amended (the

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Guarantee and Collateral Agreement), was further amended pursuant to the Reaffirmation and Amendment of Collateral Documents, dated as of September 11, 2015, by and among CIT, us, Joe s Jeans Subsidiary, Hudson, Innovo West Sales, Inc., Joe s Jeans Retail Subsidiary, Inc., Hudson Clothing Holdings, Inc., and HC Acquisition Holdings, Inc (the ***Reaffirmation and Amendment of Collateral Documents***), providing for among other things, the addition of the factor as a secured party under the Guarantee and Collateral Agreement.

Advances under the Revolving Facility are in the form of either base rate loans or LIBOR rate loans. The interest rate for base rate loans under the Revolving Commitment fluctuates and is equal to (x) the greatest (the ***Alternate Base Rate***) of (a) JPMorgan Chase Bank prime rate; (b) the Federal funds rate plus 0.50%; and (c) the rate per annum equal to the 90 day LIBOR published in the New York City edition of the Wall Street Journal under Money Rates (the ***90-Day LIBO Rate***) plus 1.0%, in each case, plus (y) 3.50%. The interest rate for LIBOR rate loans under the Revolving Commitment is equal to the 90-Day LIBO Rate per annum plus 4.50%. Interest on the Revolving Facility is payable on the first day of each calendar month and the maturity date. Among other fees, the Borrowers pay a commitment fee of 0.25% per annum (due quarterly) on the average daily amount of the unused revolving commitment under the Revolving Facility. The Borrowers also pay fees with respect to any letters of credit issued under the Revolving Facility.

The Revolving Facility contains usual and customary negative covenants for transactions of this type, including, but not limited to, restrictions on our and our subsidiaries ability, to create or incur indebtedness; create liens; consolidate, merge, liquidate or dissolve; sell, lease or otherwise transfer any of its assets (with the Asset Sale expressly permitted); substantially change the nature of its business; make investments or acquisitions; pay dividends; enter into transactions with affiliates; amend material documents, prepay certain indebtedness and make capital expenditures. The negative covenants are subject to certain exceptions as specified in the A&R Revolving Credit Agreement.

Additionally, in connection with the Asset Sale, Joe s Jeans Subsidiary, Hudson, the Operating Assets Purchaser and CIT entered into a Reassignment and Termination Agreement, dated as of September 11, 2015 (the ***Reassignment and Termination Agreement***). Pursuant to the Reassignment and Termination Agreement, Joe s Jeans Subsidiary was terminated as a party to the Amended and Restated Factoring Agreement, dated as of September 30, 2013 (as amended, the ***Amended and Restated Factoring Agreement***), by and among Joe s Jeans Subsidiary, Hudson, and CIT. Subject to the terms and conditions provided in the Reassignment and Termination Agreement, CIT reassigned to Joe s Jeans Subsidiary all of its accounts factored with CIT which were outstanding as of the date of the Reassignment and Termination Agreement.

Separation Agreement with Joseph Dahan

As previously disclosed, in connection with the closing of the Operating Asset Purchase Agreement on September 11, 2015, Mr. Joseph M. Dahan resigned as our Creative Director and Director pursuant to the Separation Agreement and Mutual Limited Release, dated as of September 8, 2015, between Mr. Dahan and us (the ***Separation Agreement and Mutual Limited Release***).

Employment Agreement with Peter Kim

On September 8, 2015, we entered into a new three-year Employment Agreement with Mr. Kim (the ***Employment Agreement***), to serve as the Chief Executive Officer of Hudson that will become effective and replace Mr. Kim s previous employment agreement as of the Effective Time. Mr. Kim s annual base salary will initially be $600,000 and Mr. Kim will also be eligible to receive an annual discretionary bonus targeted at 50% of his base salary, based on the satisfaction of criteria and performance standards as established in advance by the Compensation

Committee. The Employment Agreement also provides Mr. Kim with certain other benefits and the reimbursement of certain expenses, which are discussed in detail in the Employment Agreement. At the Effective Time, we have agreed to grant Mr. Kim (i) restricted stock units in respect of 166,667 shares of Common Stock (the ***Restricted Stock Award***) that will vest and become transferable in three equal, annual installments beginning on the first anniversary of the Effective Time, subject to Mr. Kim s continuous employment and (ii) performance share units in respect of 166,667 shares of the Common Stock (the ***Performance Shares***) that will be earned over a three-year performance period. One-third of the Performance Shares will be entitled to vest each year based on annual performance metrics established by the Compensation and Stock Option Committee of the Board at the beginning of the applicable year. The Restricted Stock Award and Performance Shares will be settled in cash, unless we attain stockholder approval of a new equity incentive plan covering such awards. Mr. Kim will also be entitled to participate in all regular long-term incentive programs maintained by us or Hudson on the same basis as similarly-situated employees.

Mr. Kim has also entered into a non-competition agreement with us and Hudson (the ***Non-Competition Agreement***), which also will become effective as of the Effective Time of the Merger, pursuant to which Mr. Kim has agreed not to engage in, compete with or permit his name to be used by or in connection with any premium denim apparel business outside his role with Hudson, that is competitive to us, Hudson or our respective subsidiaries for a period of up to three years from the Effective Time.

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NOTE 3 DISCONTINUED OPERATIONS

On September 11, 2015, we completed the Asset Sale of our Joe s Business. Accordingly, the Joe s Business was classified as held for sale as of August 31, 2015 and its results of operations are presented as discontinued operations in the accompanying condensed consolidated statements of net loss and comprehensive loss for all periods presented. The assets and liabilities of the discontinued operations have been reclassified as assets and liabilities held for sale within our condensed consolidated balance sheets for all periods presented.

The operating results of discontinued operations for the three and nine months ended August 31, 2015 and 2014 are as follows (in thousands):

	Three months ended		Nine months ended	
	August 31, 2015	August 31, 2014	August 31, 2015	August 31, 2014
	(unaudited)		(unaudited)	
Net sales	$ 22,120	$ 26,950	$ 69,965	$ 79,222
Income (loss) from discontinued operations, before provision for income taxes	(1,846)	1,036	(2,006)	3,712
Income tax expense (benefit)	(793)	272	(793)	983
Income (loss) from discontinued operations	$ (1,053)	$ 764	$ (1,213)	$ 2,729

The components of major assets and liabilities held for sale at August 31, 2015 and November 30, 2014 were as follows (in thousands):

	August 31, 2015 (unaudited)	November 30, 2014 (unaudited)
ASSETS:		
Current assets:		
Accounts receivable, net	$ 682	$ 1,309
Factored accounts receivable, net	12,014	19,316
Inventories, net	29,396	35,965
Prepaid expenses and other current assets	337	460
Property and equipment, net	1,988	
Goodwill	3,836	
Intangible assets	24,000	
Other assets	279	
Total Current assets	72,532	57,050
Noncurrent assets:		
Property and equipment, net		2,143
Goodwill		3,836
Intangible assets		24,000
Other assets		295
Total Noncurrent assets		30,274
Assets of held for sale	$ 72,532	$ 87,324
LIABILITIES:		
Current liabilities:		

Accounts payable and accrued expenses	$	4,558	$	10,854
Deferred rent		65		
Total Current liabilities		4,623		10,854
Noncurrent liabilities:				
Deferred rent				32
Total Noncurrent liabilities				32
Liabilities held for sale	$	4,623	$	10,886

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NOTE 4 ADOPTION OF ACCOUNTING PRINCIPLES

In April 2014, the Financial Accounting Standards Board, (***FASB***), issued Accounting Standards Update, (***ASU***) 2014-08, *Presentation of Financial Statements (Topic 205) and Property Plant and Equipment (Topic 360), Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity,* (***ASU 2014-08***) which provides amended guidance on the presentation of financial statements and reporting discontinued operations and disclosures of disposals of components of an entity within property, plant and equipment. ASU 2014-08 amends the definition of a discontinued operation and requires entities to disclose additional information about disposal transactions that do not meet the discontinued operations criteria. The effective date of ASU 2014-08 is for disposals that occur in annual periods (and interim periods therein) beginning on or after December 15, 2014, with early adoption permitted. We are currently evaluating the impact, if any, that this amended guidance may have on our consolidated financial statements and related disclosures.

In May 2014, FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, (***ASU 2014-09***) which provides a single, comprehensive framework for all entities in all industries to apply in the determination of when to recognize revenue, and, therefore, supersedes virtually all existing revenue recognition requirements and guidance. This framework is expected to result in less complex guidance in application while providing a consistent and comparable methodology for revenue recognition. The core principle of the guidance is that an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract(s), (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract(s), and (v) recognize revenue when, or as, the entity satisfies a performance obligation. We are currently evaluating the impact that this amended guidance will have on our consolidated financial statements and related disclosures. In July 2015, the FASB reached a decision to defer the effective date of the amended guidance. In August 2015, ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date,* was issued which defers the effective date of ASU 2014-09 to December 15, 2017. Early adoption is not permitted.

In August 2014, FASB issued ASU No. 2014-15 to communicate amendments to FASB Accounting Standards Codification Subtopic 205-40, *Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern,* (the ***ASC amendments***). The ASC amendments establish new requirements for management to evaluate a company s ability to continue as a going concern and to provide certain related disclosures. The ASC amendments are effective for the annual periods ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted, but we have not yet adopted such guidance.

In July 2015, FASB issued ASU 2015-11, *Inventory (Topic 330) - Simplifying the Measurement of Inventory*, which will require an entity to measure inventory at the lower of cost or net realizable value. Net realizable value is defined as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The guidance will be effective for us beginning with fiscal year 2018. Early adoption is permitted. We are currently evaluating the impact that this amended guidance will have on our consolidated financial statements and related disclosures.

NOTE 5 FACTORED ACCOUNTS AND RECEIVABLES

Factored accounts and receivables consist of the following (in thousands):

	August 31, 2015	**November 30, 2014**

Non-recourse receivables assigned to factor	$	11,331	$	14,314
Client recourse receivables		517		1,919
Total receivables assigned to factor		11,848		16,233
Allowance for customer credits		(3,330)		(5,128)
Due from factor	$	8,518	$	11,105
Non-factored accounts receivable	$	1,101	$	2,123
Allowance for customer credits		(788)		(766)
Allowance for doubtful accounts		(171)		(78)
Accounts receivable, net of allowance	$	142	$	1,279

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Of the total amount of receivables sold by us as of August 31, 2015 and November 30, 2014, we hold the risk of payment of $517,000 and $1,919,000, respectively, in the event of non-payment by the customers.

CIT Commercial Services Amended and Restated Factoring Agreement

On September 30, 2013, we entered into the Amended and Restated Factoring Agreement with CIT, which replaced all prior agreements relating to factoring and inventory security. The Amended and Restated Factoring Agreement provides that we sell and assign to CIT certain of our accounts receivable, including accounts arising from or related to sales of inventory and the rendition of services. We will pay a factoring rate of 0.50 percent for accounts for which CIT bears the credit risk, subject to discretionary surcharges, and 0.35 percent for accounts for which we bear the credit risk, but in no event less than $3.50 per invoice. The Amended and Restated Factoring Agreement may be terminated by CIT upon 60 days written notice or immediately upon the occurrence of an event of default as defined in the agreement. The accounts receivable agreement may be terminated by us upon 60 days written notice prior to September 30, 2018 or annually with 60 days written notice prior to September 30th of each year thereafter. The Amended and Restated Factoring Agreement remains effective until it is terminated.

In November 2014, we received an initial notice of default and event of default and demand for payment of default interest from Garrison, as term loan agent, under the term loan facility entered into on September 30, 2013. As a result of the event of default under the term loan facility, this also triggered a default and an event of default under the terms of the revolving credit facility with CIT entered into on September 30, 2013. As a result of such default and event of default, both of CIT and Garrison have reserved their respective rights to exercise any and all remedies available to them under their respective agreements and have demanded payment of interest under those agreements at the default rate of interest. On February 10, 2015, we received additional notices of default and events of default for failure to comply with certain financial and other covenants and a demand for continued payment of default interest from both Garrison and CIT.

On June 26, 2015, we entered into a CIT Forbearance Agreement with CIT as discussed above. See Note 2 - Subsequent Events for a further discussion of the Asset Sale, repayment of certain indebtedness under the agreements with Garrison and CIT and the entry into the A&R Revolving Credit Agreement.

As of August 31, 2015, our cash balance was $368,000 and our borrowing base cash availability with CIT was approximately $11,000,000. This amount with CIT fluctuates on a daily basis based upon invoicing and collection related activity by CIT for the receivables sold. See also Note 14 Debt for a further discussion of our debt arrangements with CIT and other lenders and Note 2 Subsequent Events for a discussion of our A&R Revolving Credit Agreement and the Amended and Restated Factoring Agreement with CIT.

NOTE 6 INVENTORIES, NET

Inventories are valued at the lower of cost or market with cost determined by the first-in, first-out method. Inventories consisted of the following (in thousands):

	August 31, 2015	**November 30, 2014**

Finished goods	$	9,319	$	15,478
Finished goods consigned to others		718		531
Work in progress		1,332		3,157
Raw materials		5,328		6,778
		16,697		25,944
Less reserves for obsolescence and slow moving items		(1,347)		(590)
	$	15,350	$	25,354

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NOTE 7 LONG-LIVED AND INTANGIBLE ASSETS AND GOODWILL

Valuation of Long-lived and Intangible Assets and Goodwill

We assess the impairment of identifiable intangibles, long-lived assets and goodwill annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors considered important that could trigger an impairment review other than on an annual basis include the following:

- A significant underperformance relative to expected historical or projected future operating results;
- A significant change in the manner of the use of the acquired asset or the strategy for the overall business; or
- A significant negative industry or economic trend.

When we determine that the carrying value of long-lived assets may not be recoverable based upon the existence of one or more of the aforementioned factors and the carrying value exceeds the estimated undiscounted cash flows expected to be generated by the asset, impairment is measured based on a projected discounted cash flow method using a discount rate determined by management. These cash flows are calculated by netting future estimated sales against associated merchandise costs and other related expenses such as payroll, occupancy and marketing. An asset is considered to be impaired if we determine that the carrying value may not be recoverable based upon our assessment of the asset s ability to continue to generate income from operations and positive cash flow in future periods or if significant changes our strategic business objectives and utilization of the assets occurred. If the carrying amount of an asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the estimated fair value, which is determined based on discounted future cash flows. The impairment loss calculations require management to apply judgment in estimating future cash flows and the discount rates that reflect the risk inherent in future cash flows. Future expected cash flows for store assets are based on management s estimates of future cash flows over the remaining lease period or expected life, if shorter. We consider historical trends, expected future business trends and other factors when estimating each store s future cash flow. We also consider factors such as: the local environment for each store location, including mall traffic and competition; our ability to successfully implement strategic initiatives; and the ability to control variable costs such as cost of sales and payroll, and in some cases, renegotiate lease costs.

In the third and fourth quarter of fiscal 2014, we recorded store impairment charge of $840,000 related to six of our retail stores. In the third quarter of fiscal 2015, we recorded store impairment charge of $470,000 related to two of our retail stores. Based on the operating performance of these stores, we believed that we could not recover the carrying value of property and equipment located at these stores.

Business acquisitions are accounted for under the purchase method by assigning the purchase price to tangible and intangible assets acquired and liabilities assumed. Assets acquired and liabilities assumed are recorded at their fair values and the excess of the purchase price over the amounts assigned is recorded as goodwill. Purchased intangible assets with finite lives are amortized over their estimated useful lives. Goodwill and

intangible assets with indefinite lives are not amortized but are tested at least annually for impairment or whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

In fiscal 2007, we acquired through merger JD Holdings, which included all of the goodwill and intangible assets goodwill related to the Joe s®, Joe s Jeans and JD® logo and marks. On September 30, 2013, we acquired Hudson, which included all of the goodwill and intangible assets related to the Hudson® logos and marks. We have assigned an indefinite life to the remaining intangible assets relating to the trademarks acquired, and therefore, no amortization expenses are expected to be recognized. However, we will test the assets for impairment annually in accordance with our critical accounting policies. On September 11, 2015, we sold the Intellectual Property Assets of the Joe s Business to the IP Asset Purchaser. See Note 2 - Subsequent Events for a further discussion of the sale of these and other assets.

We evaluate goodwill for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable using a two-step process. The first step is to determine the fair value of each reporting unit and compare this value to its carrying value. If the fair value exceeds the carrying value, no further work is required and no impairment loss would be recognized. The second step is performed if the carrying value exceeds the fair value of the assets. The implied fair value of the reporting unit s goodwill must be determined and compared to the carrying value of the goodwill.

We review our other indefinite-lived intangible assets for impairment on an annual basis, or when circumstances indicate their carrying value may not be recoverable. We calculate the value of the indefinite-lived intangible assets using a discounted cash flow method, based on the relief from royalty concept.

Our annual impairment testing date is September 30 of each year or when circumstances indicate their carrying value may not be recoverable. Based on our under-performance in the fourth quarter of fiscal 2014, we determined that it was appropriate to perform an impairment testing as of November 30, 2014. Based on our testing we determined that the goodwill allocated to our Hudson wholesale reporting unit was impaired by $23,585,000, and there was no impairment of our other indefinite-lived intangible assets. As of February 28, 2015, we also determined that a triggering event had occurred due to the decline in our market capitalization and tested our goodwill and other indefinite-lived assets for impairment and determined that there was no impairment.

NOTE 8 RELATED PARTY TRANSACTIONS

Joe Dahan

Since the acquisition of the Joe s® brand as a result of a merger in October 2007 through February 18, 2013, Mr. Dahan was entitled to a certain percentage of our gross profit in any applicable fiscal year until October 2017. At the time of the acquisition, pursuant to ASC 805 *Business Combinations,* we assessed this original contingent consideration arrangement as compensatory and expensed such amounts over the term of the earn out period at the defined percentage amounts.

On February 18, 2013, we entered into a new agreement with Mr. Dahan that fixed the overall amount to be paid by us for the remaining months of year six through year 10 in the original merger agreement at $9,168,000 through weekly installment payments beginning on February 22, 2013 until November 27, 2015. In the first quarter of fiscal 2013, we recorded a charge of $8,732,000 as contingent consideration buy-out expense in connection with this agreement. This amount represented the net present value of the total fixed amount that Mr. Dahan would receive. The entire amount was expensed during the first quarter of fiscal 2013 as the amount payable represented a present obligation due to Mr. Dahan. On September 30, 2013, in connection with entry into new credit facilities relating to the acquisition of Hudson, Mr. Dahan, CIT, Garrison and all of our loan parties entered into an earn out subordination agreement, which provides, among other things, that any payment, whether in cash, in kind, securities or any other property, in connection with the our obligations to Mr. Dahan is expressly junior and subordinated in right of payment to all amounts due and owing upon any indebtedness outstanding under the revolving credit facility and the term loan facility. We were permitted to make certain amounts of weekly installment payments of our obligations in the absence of an insolvency proceeding or any event of default under the revolving credit agreement or the term loan credit agreement. As a result of our default under the revolving credit agreement or the term loan credit agreement, we did not make any payments to Mr. Dahan during fiscal 2015. In connection with the Asset Sale, Mr. Dahan was repaid a portion of the payments owed to him and the remainder is expected to be paid at the closing of the Merger and Merger Transactions.

See Note 12 Commitments and Contingencies - Contingent Consideration Payments, Buy Out Agreement and Earnout Subordination Agreement for a further discussion on these agreements with Mr. Dahan and Note 2 Subsequent Events for a discussion of Mr. Dahan s termination of employment and resignation from our Board of Directors.

Ambre Dahan

In January 2013, we entered in to a consulting arrangement with Ambre Dahan, the spouse of Mr. Dahan, for design director services that paid her $175,000 per annum on a bi-weekly basis. For the three months ended August 31, 2015 and 2014, we paid Ms. Dahan $0 and $47,000, and for the nine months ended August 31, 2015 and 2014, we paid Ms. Dahan $0 and $135,000, respectively, under this arrangement. This arrangement was terminated effective as of November 17, 2014.

Albert Dahan

In October 2011, we entered into an agreement with Ever Blue LLC (***Ever Blue***), an entity for which Albert Dahan is the sole member, for the sale of children s products. Ever Blue has an exclusive right to produce, distribute and sell children s products bearing the Joe s® brand on a worldwide basis, subject to certain limitations on the channels of distribution. In exchange for the license, Ever Blue pays to us a royalty on net sales with certain guaranteed minimum sales for each term. In connection with this agreement, we provided initial funding to Ever Blue for inventory purchases, which such amount has been repaid in full. For the three months ended August 31, 2015 and 2014, we recognized $0 and $52,000, respectively, in royalty income under the license agreement. For the nine months ended August 31, 2015 and 2014, we recognized $45,000 and $360,000, respectively, in royalty income under the license agreement.

Peter Kim

We have entered into several agreements, including a stock purchase agreement, a convertible note, a registration rights agreement, an employment agreement and a non-competition agreement with Peter Kim, Chief Executive Officer of our Hudson subsidiary, in connection with the acquisition of Hudson. See Note 14 - Debt for a further discussion of those agreements. In connection with the Merger, we entered into the Rollover Agreement, the Employment Agreement and the Non-Competition Agreement. For a description of those agreements see Note 2 - Subsequent Events

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Employment Agreements with Officers and Directors

We have entered into employment agreements with Marc Crossman, our former President and Chief Executive Officer, Joe Dahan, our former Creative Director, Peter Kim, our Chief Executive Office of our Hudson subsidiary, and Hamish Sandhu, our Chief Financial Officer. Mr. Dahan was also a member of our Board of Directors until September 11, 2015.

Marc Crossman

On May 30, 2008, we entered into an employment agreement with Mr. Crossman to serve as our President and Chief Executive Officer. The employment agreement was effective as of December 1, 2007, the commencement of our 2008 fiscal year, had an initial term of two years and automatically renewed for additional two year periods on December 1, 2009, December 1, 2011 and December 1, 2013, respectively. The employment agreement continues to automatically renew for additional two year periods if neither we nor Mr. Crossman provides 180 days advanced notice of non-renewal prior to the end of the term or upon the occurrence of a change in control. Under the employment agreement, Mr. Crossman is entitled to an annual salary of $429,300, an annual discretionary bonus targeted at 50 percent of his base salary based upon the achievement of financial and other performance criteria that the Compensation and Stock Option Committee of the Board of Directors, or Compensation Committee, may deem appropriate in its sole and absolute discretion, an annual grant of equity compensation pursuant to our stock incentive plans, life and disability insurance policies paid on his behalf and other discretionary benefits that the Compensation Committee may deem appropriate in its sole and absolute discretion. The employment agreement provides for severance payment of up to two years if terminated under certain circumstances.

On January 19, 2015, our Board of Directors accepted the resignation of Mr. Crossman. The Board and Mr. Crossman also agreed that Mr. Crossman would become a consultant for a period of twelve (12) months pursuant to a consulting agreement. In exchange for a release of all claims related to Mr. Crossman s employment and the provision of consulting services by Mr. Crossman, we have agreed to pay Mr. Crossman the following: (i) payment of $35,775 per month for a period of twelve (12) months; (ii) acceleration of the unvested equity awards previously granted to Mr. Crossman; (iii) granted him restricted common stock in the amount of 600,000 shares that vest 1/12th on a monthly basis over the twelve (12) month period; and (iv) agreed to reimburse him for health and dental COBRA payments for a period of twelve (12) months or until he is eligible for coverage under a successor employer s group health plan.

Joe Dahan

On October 25, 2007, we entered into an employment agreement for Mr. Dahan to serve as Creative Director for the Joe s brand. The initial term of employment was for five years, or until October 25, 2012, and then automatically renewed for successive one year periods unless terminated earlier in accordance with the agreement. Under the employment agreement, Mr. Dahan is entitled to an annual salary of $300,000 and other discretionary benefits that the Compensation Committee may deem appropriate in its sole and absolute discretion. The employment agreement provides for severance payment of up to one year if terminated under certain circumstances. In connection with the separation and mutual release agreement entered into with Mr. Dahan, we agreed to pay him severance from September 11, 2015 until October 25, 2015. See Note 2 Subsequent Events for a discussion of the agreement.

Peter Kim

On September 30, 2013, we entered into an employment agreement with Mr. Kim to serve as Chief Executive Officer of our Hudson subsidiary for a term of three years. Under the employment agreement, Mr. Kim is entitled to a base salary of $500,000 per year and is also eligible to receive an annual discretionary bonus targeted at 50 percent of his base salary, based on the satisfaction of criteria and performance standards as established in advance and agreed to by Mr. Kim and the Compensation Committee. Mr. Kim is also entitled to other discretionary benefits that the Compensation Committee may deem appropriate in its sole and absolute discretion. The employment agreement provides for severance payment of up to one year if terminated under certain circumstances. In connection with the Merger, we entered into the Employment Agreement and Non-Competition Agreement with Mr. Kim to be effective upon the completion of the Merger. See Note 2 Subsequent Events for details of the agreement.

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Hamish Sandhu

On July 2, 2015, we entered into an employment agreement with Mr. Sandhu to serve as our Chief Financial Officer for a term of one year with automatic renewal for successive one year periods unless terminated earlier in accordance with the agreement or advanced notice of non-renewal 90 days before the expiration of the current term. Under the employment agreement, Mr. Sandhu is entitled to a an annual salary of $325,000 and other cash and non-cash compensation, including an annual discretionary cash and equity bonus of not less than 10 percent of his base salary based upon the achievement of financial and other performance criteria as set forth in the employment agreement, premiums for health insurance paid on his behalf and for his family and life and disability insurance policies paid on his behalf. The employment agreement provides for severance payment of up to one year if terminated under certain circumstances.

NOTE 9 EARNINGS PER SHARE

Earnings per share are computed using weighted average common shares and dilutive common equivalent shares outstanding. Potentially dilutive shares consist of outstanding options, shares issuable upon the assumed conversion of Convertible Notes, restricted stock and unvested restricted stock units (***RSUs***) A reconciliation of the numerator and denominator of basic earnings per share and diluted earnings per share is as follows:

	Three months ended (in thousands, except per share data)		Nine months ended (in thousands, except per share data)	
	August 31, 2015	**August 31, 2014**	**August 31, 2015**	**August 31, 2014**
Basic earnings (loss) per share computation:				
Numerator:				
Income (loss) from continuing operations	$ 6,712	$ (488)	$ (18,072)	$ (2,292)
Income (loss) from discontinued operatoins	(1,053)	764	(1,213)	2,729
Net income (loss) and comprehensive (loss) income	$ 5,659	$ 276	$ (19,285)	$ 437
Denominator:				
Weighted average common shares outstanding	69,614	68,362	69,314	68,151
Income (loss) per common share - basic				
Income (loss) from continuing operations	$ 0.10	$ (0.01)	$ (0.26)	$ (0.03)
Income (loss) from discontinued operatoins	(0.02)	0.01	(0.02)	0.04
Net (loss) income and comprehensive (loss) income	$ 0.08	$ 0.00	$ (0.28)	$ 0.01
Diluted earnings (loss) per share computation:				
Numerator:				
Income (loss) from continuing operations	$ 6,712	$ (488)	$ (18,072)	$ (2,292)
Income (loss) from discontinued operatoins	(1,053)	764	(1,213)	2,729
Net income (loss) and comprehensive (loss) income	$ 5,659	$ 276	$ (19,285)	$ 437
Denominator:				
Weighted average common shares outstanding	69,614	68,362	69,314	68,151
Effect of dilutive securities:				
Restricted shares, RSU s and options	6	518		784
Dilutive potential common shares	69,620	68,880	69,314	68,935

Income (loss) per common share - dilutive								
Income (loss) from continuing operations	$	0.10	$	(0.01)	$	(0.26)	$	(0.03)
Income (loss) from discontinued operatoins		(0.02)		0.01		(0.02)		0.04
Net income (loss) and comprehensive (loss) income	$	0.08	$	0.00	$	(0.28)	$	0.01

For the three months ended August 31, 2015, and 2014, currently exercisable options, the Convertible Notes, unvested restricted shares and unvested RSUs in the aggregate of 19,840,873 and 19,656,831, respectively, have been excluded from the calculation of the diluted loss per share as their effect would have been anti-dilutive.

For the nine months ended August 31, 2015, and 2014, currently exercisable options, the Convertible Notes, unvested restricted shares and unvested RSUs in the aggregate of 19,882,230 and 19,766,669, respectively, have been excluded from the calculation of the diluted loss per share as their effect would have been anti-dilutive.

Shares Reserved for Future Issuance

As of August 31, 2015, shares reserved for future issuance include: (i) 88,333 shares of common stock issuable upon the exercise of stock options granted under the incentive plans; (ii) 448,103 shares of common stock issuable upon the vesting of RSUs; (iii) an aggregate of 2,642,271 shares of common stock available for future issuance under the Amended and Restated 2004 Stock Incentive Plan; and (iv) 19,095,794 shares of common stock issuable pursuant to the Convertible Notes.

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NOTE 10 INCOME TAXES

A valuation allowance is required when it is more likely than not that all or a portion of a deferred tax asset will not be realized. Quarterly, management reassesses the need for a valuation allowance. Realization of deferred income tax assets is dependent upon taxable income in prior carryback years, estimates of future taxable income, tax planning strategies and reversals of existing taxable temporary differences. In determining the need for a valuation allowance, we reviewed all available evidence pursuant to the requirements of FASB ASC 740. Pursuant to ASC 740, we excluded the deferred income tax liabilities associated with identified indefinite long lived intangible assets as a source of income. For the first quarter of fiscal 2015, based upon our assessment of all available evidence, we have concluded that it is more likely than not that the net deferred tax assets, as of November 30, 2014, with the exception of certain deferred taxes associated with separate filing states for Hudson, will not be realized. For the first quarter of fiscal 2015, the valuation allowance associated with deferred taxes as of November 30, 2014, increased by $14,481,000. Based on our prior assessment for fiscal 2014, 2013, and 2012, we had determined that the deferred tax assets were more likely than not to be realized with the exception of a valuation allowance of $640,000, $342,000 and $0, respectively, that was recorded against a state net operating loss deferred tax asset. We considered all available evidence, both positive and negative, in our assessment of the valuation allowance needed as of February 28, 2015. Due to a review of operating performance for the quarter and a change in business strategy, which included the disposal of certain assets that have a fair value in excess of tax basis, we increased our valuation allowance by $14,481,000 as of February 28, 2015. In calculating the amount of deferred tax assets subject to a valuation allowance, we have excluded the deferred tax liabilities associated with our trademarks from that amount. These intangible assets have an indefinite life and therefore, we cannot expect that the associated deferred tax liabilities will reverse over the same periods as our other net deferred tax assets. For the third quarter of fiscal 2015, based on our reassessment of the realizability of deferred taxes, due to the September 11, 2015 asset sale described in Note 2, the valuation allowance established during the first quarter is reduced by $6,528,000. We determined that the net deferred taxes associated with that valuation allowance reduction (excluding the deferred tax liabilities for trademarks) were realized as part of the asset sale. The tax benefit for the three months ended August 31, 2015 consisted of the discrete reduction of $6,528,000 to our valuation allowance established during the first quarter of fiscal 2015 and the recording of the tax benefit for the operating losses for the nine months ended August 31, 2015 for which no tax benefit was previously taken.

NOTE 11 STOCKHOLDERS EQUITY

Stock Incentive Plans

On June 3, 2004, we adopted the 2004 Stock Incentive Plan (the ***2004 Incentive Plan***) and in October 2011, we adopted an Amended and Restated 2004 Stock Incentive Plan (the ***Restated Plan***) to update it with respect to certain provisions and changes in the tax code since its original adoption. Under the Restated Plan, the number of shares authorized for issuance is 6,825,000 shares of common stock. After the adoption of the Restated Plan in October 2011, we no longer grant awards pursuant to the 2004 Incentive Plan; however, it remains in effect for awards outstanding as of the adoption of the Restated Plan. Under the Restated Plan, grants may be made to employees, officers, directors and consultants under a variety of awards based upon underlying equity, including, but not limited to, stock options, restricted common stock, restricted stock units or performance shares. The Restated Plan limits the number of shares that can be awarded to any employee in one year to 1,250,000. The exercise price for incentive options may not be less than the fair market value of our common stock on the date of grant and the exercise period may not exceed ten years. Vesting periods, terms and types of awards are determined by the Board of Directors and/or our Compensation Committee. The Restated Plan includes a provision for the acceleration of vesting of all awards upon a change of control as well as a provision that allows forfeited or unexercised awards that have expired to be available again for future issuance. Since fiscal 2008, we have issued both restricted common stock and RSUs to our officers, directors and employees pursuant to our various plans. The RSUs represent the right to receive one share of common stock for each unit on the vesting date provided that the employee continues to be employed by us. On the vesting date of the RSUs, we expect to issue the shares of common stock to each participant upon vesting and expect to withhold an equivalent number of shares at fair market value on the vesting date to fulfill tax withholding obligations. Any RSUs withheld or forfeited will be shares available for issuance in accordance with the terms of the Restated Plan.

The shares of common stock issued upon exercise of a previously granted stock option or a grant of RSUs are considered new issuances from shares reserved for issuance in connection with the adoption of the various plans. We require that the option holder provide a written notice of exercise in accordance with the option agreement and plan to the stock plan administrator and full payment for the shares be made prior to issuance. All issuances are made under the terms and conditions set forth in the applicable plan. As of August 31, 2015, 2,642,271 shares remained available for issuance under the Restated Plan.

For all stock compensation awards that contain graded vesting with time-based service conditions, we have elected to apply a straight-line recognition method to account for all of these awards. For existing grants that were not fully vested at November 30, 2014, there was a total of $1,206,000 and $938,000 of stock based compensation expense recognized during the nine months ended August 31, 2015 and 2014, respectively.

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The following summarizes option grants, restricted common stock and RSUs issued to members of the Board of Directors for the fiscal years 2002 through the third quarter of fiscal 2015 (in actual amounts) for service as a member:

Granted as of:	August 31, 2015 Number of options	Exercise price
2002	40,000	$ 1.00
2002	31,496	$ 1.27
2003	30,768	$ 1.30
2004	320,000	$ 1.58