BODY CENTRAL CORP
Form 10-Q
November 06, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 27, 2014

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 001-34906

BODY CENTRAL CORP.
(Exact name of registrant as specified in its charter)

Delaware	14-1972231
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

6225 Powers Avenue
Jacksonville, FL 32217
(Address, including zip code, of principal executive offices)

Registrant’s telephone number, including area code: (904) 737-0811

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 ý No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý 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. (Check one):

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 in Rule 12b-2 of the Exchange Act.)
Yes o No ý

The number of shares outstanding of the registrant’s common stock as of November 3, 2014 was 1,921,135 shares.

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On September 4, 2014, Body Central Corp. (herein “we”, “our”, “us”, or the “Company”) implemented, pursuant to stockholder authorization, a 1-for-10 reverse stock split of the Company’s common stock, which became effective for trading purposes on September 9, 2014. All share and per share amounts of common stock and options in the accompanying financial statements have been restated for all periods to give retroactive effect to the reverse stock split.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements concerning our business, operations and financial performance and condition as well as our plans, objectives and expectations for our business operations and financial performance and condition, all of which are subject to risks and uncertainties. All statements other than statements of historical fact included in this Quarterly Report on Form 10-Q are forward-looking statements. You can identify these statements by words such as “aim,” “anticipate,” “assume,” “believe,” “could,” “due,” “estimate,” “expect,” “goa “may,” “objective,” “plan,” “potential,” “positioned,” “predict,” “project,” “should,” “target,” “will,” “would” and other simila that are predictions of, or indicate future events and future trends. These forward-looking statements are based on current expectations, estimates, forecasts and projections about our business and the industry in which we operate and our management’s beliefs and assumptions. These statements are not guarantees of future performance or development and involve known and unknown risks, uncertainties and other factors that are in some cases beyond our control. All forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those that we expected; some important factors include, but are not limited to, the following:

- expectations regarding our ability to continue as a going concern;
- our ability to achieve and maintain the required base amount of unrestricted cash to eliminate the existing cash dominion event, or otherwise trigger an event of default under the terms of our senior credit facility, as amended;
- our failure to register our common stock under the Registration Rights Agreement, resulting in material penalties related to our Subordinated Secured Convertible Notes;
- a sale or issuance of our common stock at a price less than the conversion price under the Subordinated Secured Convertible Notes agreement triggering an anti-dilution provision;
- the potential for acceleration of any of our indebtedness, the potential that cross-default provisions under our first lien credit facility and second lien note instruments could be triggered, as well as any trigger by an event of default of cash dominion provisions under our first lien credit facility;
- our ability to obtain financing or to generate sufficient cash flows to support operations;
- our ability to identify and respond to new and changing fashion trends, customer preferences and other related factors;
- the dislocation of customers that may occur as a result of strategic changes to marketing or merchandise selections;
- failure to successfully execute marketing initiatives to drive core customers into our stores and to our website;
- failure to successfully execute our growth strategy;
- changes in consumer spending and general economic conditions;
- changes in Federal and state tax policy on our customers;
- changes in the competitive environment in our industry and the markets we serve, including increased competition from other retailers;
- failure of our stores to achieve sales and operating levels consistent with our expectations;
- failure to successfully execute our direct business unit initiatives;
- our dependence on a strong brand image;
- failure of our information technology systems to support our business;
- failure to successfully integrate new information technology systems to support our business;
- our dependence upon key executive management or our inability to hire or retain additional personnel;
- changes in payments terms, including reduced credit limits and/or requirements to provide advance payments to our vendors;
- disruptions in our supply chain and distribution facility;

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- our reliance upon independent third-party transportation providers for all of our product shipments;
- hurricanes, natural disasters, unusually adverse weather conditions, boycotts and unanticipated events;
- the seasonality of our business;
- increases in the costs of fuel, or other energy, transportation or utilities costs as well as in the costs of raw materials, labor and employment;
- the impact of governmental laws and regulations, including tax policy, and the outcomes of legal proceedings;
- restrictions imposed by lease obligations on our current and future operations;
- our ability to resolve the Imeson lease on terms that are favorable to us;
- our failure to maintain effective internal controls; and
- our inability to protect our trademarks or other intellectual property rights.

Body Central Corp. (herein “we”, “our”, “us”, or the “Company”) derives many of its forward-looking statements from its operating budgets and forecasts, which are based upon many detailed assumptions. While we believe that our assumptions are reasonable, we caution that it is very difficult to predict the impact of known factors, and, it is impossible for us to anticipate all factors that could affect our actual results. For the discussion of these risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to “Risk Factors” herein and in our Annual Report on Form 10-K for the fiscal year ended December 28, 2013 filed with the Securities and Exchange Commission (“SEC”). The forward-looking statements included in this Quarterly Report on Form 10-Q are made only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events or otherwise, except as otherwise required by law.

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ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

BODY CENTRAL CORP.

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	Fiscal Periods Ended		
	September 27, 2014	December 28, 2013	September 28, 2013
	(in thousands, except share data)		
Assets			
Current assets			
Cash and cash equivalents	$4,850	$ 16,513	$ 15,597
Short-term investments	—	—	4,356
Restricted cash	3,153	—	—
Accounts receivable	721	2,803	1,479
Income tax receivable	826	14,802	9,373
Insurance recoverable	3,425	—	—
Inventories	12,077	18,807	24,464
Prepaid expenses and other current assets	10,370	2,055	2,848
Deferred tax asset	3,301	3,323	3,289
Total current assets	38,723	58,303	61,406
Property and equipment, net of accumulated depreciation of $36,093, $32,463, and $30,358	29,345	45,732	40,479
Goodwill	—	—	11,150
Intangible assets	7,790	16,574	16,574
Other assets	291	353	333
Total assets	76,149	120,962	129,942
Liabilities and Stockholders' Equity			
Current liabilities			
Merchandise accounts payable	1,980	8,972	10,585
Accrued expenses and other current liabilities	16,922	24,623	21,155
Legal settlement payable	3,425	—	—
Fair value of call option derivative embedded in convertible notes payable	6,925	—	—
Financing obligation, sale-leaseback, current portion	767	737	—
Total current liabilities	30,019	34,332	31,740
Other liabilities	9,039	11,358	10,167
Financing obligation, sale-leaseback, net of current portion	1,790	2,369	—
Notes payable	12,000	5,000	—
Convertible notes payable	5,589	—	—
Deferred tax liability	3,085	6,913	4,392
Total liabilities	61,522	59,972	46,299
Stockholders' equity			
Preferred stock, $0.001 par value, 5,000,000 shares authorized; 16 shares issued and outstanding			
Series A preferred stock, $0.001 par value, 3 shares authorized, issued, and outstanding as of September 27, 2014. There were no Series A preferred shares authorized, issued, or outstanding as of December 28, 2013 or September 28, 2013.	—	—	—
	—	—	—

Series B preferred stock, $0.001 par value, 13 shares authorized, issued, and outstanding as of September 27, 2014. There were no Series B preferred shares authorized, issued, or outstanding as of December 28, 2013 or September 28, 2013.			
Common stock, $0.001 par value, 45,000,000 shares authorized, 1,921,145 shares issued and outstanding as of September 27, 2014, 1,663,112 shares issued and outstanding as of December 28, 2013, and 1,664,904 shares issued and outstanding as of September 28, 2013.	2	2	2
Additional paid-in capital	99,620	99,000	98,396
Accumulated deficit	(84,995)	(38,012)	(14,755)
Accumulated other comprehensive income, net of tax	—	—	—
Total stockholders’ equity	14,627	60,990	83,643
Total liabilities and stockholders’ equity	$76,149	$ 120,962	$ 129,942

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

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BODY CENTRAL CORP.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS (UNAUDITED)

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
	(in thousands, except share data)			
Net revenues	$43,420	$60,833	$159,640	$217,383
Cost of goods sold, including occupancy, buying, distribution center and catalog costs	33,785	49,692	122,269	157,977
Gross profit	9,635	11,141	37,371	59,406
Selling, general and administrative expenses	17,276	24,480	65,990	69,406
Depreciation and amortization	2,270	2,154	6,704	6,438
Impairment of depreciable long-lived assets	9,313	—	11,197	—
Impairment of goodwill	—	—	—	10,358
Impairment of trade name	5,110	—	8,784	—
Loss from operations	(24,334)	(15,493)	(55,304)	(26,796)
Interest expense	(1,232)	(78)	(1,914)	(274)
Interest income	18	80	36	285
Change in fair value of embedded derivative liabilities	6,253	—	6,253	—
Other income (expense), net	205	(259)	140	747
Loss before income taxes	(19,090)	(15,750)	(50,789)	(26,038)
Benefit from income taxes	2,377	6,769	3,806	6,985
Net loss	$(16,713)	$(8,981)	$(46,983)	$(19,053)
Net loss per common share:				
Basic	$(10.17)	$(5.49)	$(28.70)	$(11.68)
Diluted	$(10.17)	$(5.49)	$(28.70)	$(11.68)
Weighted-average common shares outstanding:				
Basic	1,643,422	1,636,363	1,636,774	1,631,805
Diluted	1,643,422	1,636,363	1,636,774	1,631,805
Other comprehensive income:				
Other comprehensive income, net of tax	—	—	—	3
Comprehensive loss	$(16,713)	$(8,981)	$(46,983)	$(19,050)

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

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BODY CENTRAL CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Thirty-Nine Weeks Ended	
Q Dates:	September 27, 2014	September 28, 2013
	(in thousands)	
Cash flows from operating activities		
Net loss	$(46,983)	$(19,053)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	6,704	6,438
Deferred income taxes	(3,806)	(2,236)
Excess tax benefits from stock-based compensation	—	(39)
Stock-based compensation	621	2,061
Amortization of premiums and discounts on investments, net	—	147
Amortization of deferred financing costs	(351)	—
Change in fair value of derivatives	(6,253)	—
Derivative interest expense	767	—
(Gain) Loss on disposal of property and equipment	(3)	422
Impairment of long-lived assets	19,981	10,358
Changes in assets and liabilities:		
Accounts receivable	2,082	3,231
Inventories	6,730	(1,493)
Prepaid expenses and other assets	(4,896)	(5,342)
Merchandise accounts payable	(6,992)	(3,130)
Accrued expenses and other current liabilities	(4,492)	362
Income taxes	13,976	—
Other liabilities	(2,320)	(380)
Net cash used in operating activities	(25,235)	(8,654)
Cash flows from investing activities		
Payments for purchases of property and equipment	(4,682)	(12,709)
Purchases of short-term investments	—	(12,786)
Proceeds from sales of short-term investments	—	2,310
Proceeds from maturities of short-term investments	—	5,973
Change in restricted cash	(3,153)	—
Net cash used in investing activities	(7,835)	(17,212)
Cash flows from financing activities		
Payments on sale-leaseback transaction	(548)	—
Payments on line of credit	(5,000)	—
Proceeds from long-term debt	30,000	—
Proceeds from exercise of stock options	—	327
Deferred financing fees	(3,045)	—
Net cash provided by financing activities	21,407	327
Net decrease in cash and cash equivalents	(11,663)	(25,539)
Cash and cash equivalents		
Beginning of year	16,513	41,136
End of period	$4,850	$15,597

Non-cash investing activities:

Property and equipment acquired	$—	$1,114

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

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NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Nature of Business and Summary of Significant Accounting Policies

Nature of Business and Organization

Body Central Corp. (the ‘‘Company’’) is a specialty retailer of young women’s apparel and accessories operating retail stores in the South, Southwest, Mid-Atlantic and Midwest regions of the United States. The Company operates specialty apparel stores under the Body Central and Body Shop banners as well as a direct business unit marketed through the www.bodycentral.com website.

Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared assuming that the Company will continue as a going concern, which contemplates continuity of operations, the realization of assets and the satisfaction of liabilities in the normal course of business. These unaudited condensed consolidated financial statements do not include any adjustments that might result from the occurrence of any of the uncertainties described below.

The Company's results of operations during the first three fiscal quarters of 2014, including operating revenues and operating cash flows, have been negatively impacted by a number of factors including a continued decline in sales resulting from the Company's failure to adequately anticipate its target customers' preferences and demand level, minimal trade support, competitive industry conditions, and an increase in year to date expenses associated with the financing, transactional and strategic alternatives initiatives announced in April 2014. The Company has continued to experience decreased demand in both its stores and direct business operating units in the thirteen weeks ended September 27, 2014, and continues to make merchandise prepayments to a majority of its vendors prior to the processing and delivery of merchandise to its distribution facility. These factors had a significant negative impact on the Company's operating results and cash flows during the first three fiscal quarters of 2014, and the Company believes that these factors may continue to have a negative impact on its business. These conditions raise substantial doubt about the Company's ability to continue as a going concern. For this purpose, the Company assumes that a business is generally considered to be a going concern if there is neither the intention nor the need to liquidate or materially curtail the scope of its business plans.

The Company has historically relied on cash flows from operations to meet its cash flow requirements for continued operations and capital projects; however, during the first three fiscal quarters of 2014, the Company entered into financing arrangements to supplement its working capital needs including a $17.0 million senior secured credit facility and the issuance of $18.0 million in subordinated secured convertible notes (which we sometimes refer to as the "Notes"), both of which mature in fiscal 2017. As discussed further in Note 5. Debt, the Company is subject to certain provisions under its senior secured credit facility which, in the event of a default by the Company, could result in a cash dominion event. The cash dominion event is not considered an event of default under the Credit Facility Agreement, as amended. In June 2014, the Company was in default of certain provisions under its senior secured credit facility which resulted in a cash dominion event. On June 27, 2014, the debt holder provided a waiver of the defaults under the credit facility agreement and the Company was in compliance with the provisions of the credit facility agreement, as amended, as discussed further in Note 5. Debt. The Company is subject to certain provisions under its Notes and the accompanying agreements (collectively, the "Agreements"), which require the Company to register for resale by the holders of the Notes ("the Noteholders") the shares of its common stock issuable upon conversion of the Notes. The Company filed a Registration Statement on Form S-1 on September 24, 2014 for this purpose, which registration statement has not yet been declared effective by the Commission. Under the Agreements, the Company is required to use its reasonable best efforts to cause the registration statement to become effective. If the Company fails to satisfy its registration obligations within the agreed upon time frame, subject to the terms of the Intercreditor and Subordination Agreement defining the rights as between the Company’s senior secured credit facility lenders and the Noteholders, the Company will be subject to cash penalties of 2% of the aggregated purchase price, payable immediately, as well as 2% cash penalties every thirtieth day until remedied, up to a maximum of 15%. As of September 27, 2014, the Company has sufficient shares to fulfill the conversion, but had not competed the registration process. The Company's stockholders approved a 1-for-10 reverse stock split on September 4, 2014, which was implemented on that date and effective for trading purposes on September 9, 2014. On July 15, 2014, the Company entered into an amendment with the Noteholders, as discussed in Note 5. Debt, which redefined the "Initial Filing Deadline" to file the registration statement from 20 calendar days from the effective date of the initial agreement to 20 calendar days after stockholder approval was obtained for the 1-for-10 reverse stock split and to include language that eliminates the penalty fee provision associated with any failure to timely register the required number of shares to the extent that the number of shares available under the registration statement is sufficient to cover the lesser of (1) at least 100% of the maximum amount of conversion shares underlying the notes or (2) the lesser of the maximum number of shares of common stock of the Company permitted to be registered by the SEC or authorized pursuant to the Company's certificate of incorporation. The Company was in default of its debt agreements on August 12, 2014, due to an untimely filing of its Form 10-Q, for which a waiver was obtained. However, the Company is currently in compliance with both the Agreements, as amended, and the Senior Credit Facility, as amended, as all obligations have been met or waived as of the filing of this Form 10-Q. Should the Company fail to comply with the provisions of its senior secured credit facility and/or its subordinated secured convertible notes agreements, the Company will not have sufficient funds to service its debt service obligations.

Both the Credit Agreement with Crystal Financial LLC ("Crystal"), as amended, and the Notes issued, as amended, provide for cross-default in the event of certain failures to make payments when due on other material indebtedness, or failures to otherwise perform under the terms of such material indebtedness resulting in certain acceleration rights or events. In addition, the Company's first and second lien instruments provide for various other events of default, including, among others, non-compliance with material contracts (subject to certain exceptions, including where the non-compliance would not be expected to cause an event of default or termination right under the material contract). As a result, in the event the Company fails to comply with the provisions of either the first or second lien instruments, and an event of default were to be triggered, a cross-default may also arise under the other facility. Further, failures to observe other covenants in the transaction documents, including compliance with material contracts, could also result in defaults under both the Credit Agreement and the Notes. In either event, Crystal and, subject to the intercreditor and subordination agreement, the Noteholders, may have the right to accelerate the debt.

The Company believes that its current sources of funding and cash provided by operations, combined with actions discussed in more detail below, will be sufficient to fund its current business plan and meet its obligations for the twelve months through September 27, 2015; however, the Company's ability to continue to fund operations and meet its obligations is largely dependent on its ability to remain compliant with the above financing requirements, to implement its merchandising strategy and gauge the fashion tastes of its customers, to provide merchandise that satisfies customer demand and to return to more favorable trade terms. The Company has continued to move forward with refinements to its merchandising strategy which focuses on the allocation of product assortment and inventory management. However, the Company's failure to anticipate, identify, or react to changes in customer taste and demand could adversely affect its results of operations, including its ability to generate positive cash flows from operations, and consequently, its ability to fund operations, to obtain additional financing, and to repay its financing obligations. These matters raise substantial doubt about the Company's ability to continue as a going concern.

Based on the Company's current cash projections and certain requirements under the Crystal Credit LLC agreement, the Company may be subject to a cash dominion event as defined in the Crystal Credit Agreement dated February 6, 2014, as amended. On September 2, 2014, a cash dominion event was triggered as a result of our unrestricted cash falling below $7.5 million for two consecutive business days. As a result, until such time as our unrestricted cash exceeds $7.5 million for 60 consecutive calendar days, as to which there can be no assurance, inbound cash receipts will be controlled by Crystal. As the cash dominion event is not considered an Event of Default under the Credit Facility Agreement, the Company will continue to be allowed to borrow thereunder, subject to the other terms and conditions of the Credit Facility Agreement. The Company remained in dominion as of November 6, 2014.

In addition to its sales and inventory planning and management initiatives, the Company has taken several other actions to increase its liquidity which it believes should be adequate to finance its working capital needs throughout the twelve months subsequent to the quarter ended September 27, 2014. Actions taken have included cost reductions such as closing underperforming stores, headcount reductions, a reduction in travel expenses, supplies, and other general and administrative costs, and delaying non-essential capital projects until such time as the Company can generate sufficient cash flows from operations to fund its capital expenditures. The Company has also aggressively reduced and refined merchandising assortments to be more commensurate with sales volumes and improved inventory productivity goals. The Company has determined that it will stay in its current location and defer the implementation of new systems. The Company believes that its product strategy, combined with recent and ongoing cost reduction initiatives, will help to improve cash flows from operations. There can be no assurance that the Company will be successful in its implementation of these initiatives. Should the Company fail to successfully execute on its strategies, its cash flows would be materially adversely impacted, and consequently the Company may not be able to continue as a going concern. The unaudited condensed consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

During the first three fiscal quarters of 2014, significant changes impacting the Company's liquidity position have included the following:

- The Company closed 22 stores during the thirty-nine weeks ended September 27, 2014 and intends to close six more stores during the remainder of fiscal year 2014.

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- The Company received a total of $13.9 million during the first quarter of 2014 in federal income tax refunds resulting primarily from a net operating loss carryback of 2013 losses to fiscal years 2011 and 2012.
- On February 6, 2014, the Company entered into a new asset based credit facility agreement (the "Credit Facility Agreement") with Crystal Financial Corp. which provided for a $17.0 million senior secured credit facility, which included a term loan facility of $12.0 million advanced on the closing date and a revolving credit facility of $5.0 million. Additionally, the Credit Facility Agreement provided for an uncommitted term loan facility of up to $7.0 million. The Credit Facility Agreement will mature on February 6, 2017 and is secured by substantially all of the Company's assets. The proceeds of the term loan facility were used to pay all amounts owed under the Company's prior $5.0 million credit facility, to pay certain related fees and expenses, to fund working capital and for other corporate purposes.

Effective June 23, 2014, the Company entered into a Forbearance and Modification Agreement ("Forbearance Agreement") which effectively converted and increased the above outstanding term loan facility into a revolving credit facility of $17.0 million. Pursuant to the Forbearance Agreement, the Company prepaid the term loan facility in full from (i) cash on hand in excess of amounts permitted under the Forbearance Agreement plus (ii) the proceeds from the revolving credit facility. The Company was not required to pay any prepayment penalties under the terms of the Forbearance Agreement. As of the effective date of the Forbearance Agreement, the Company was in default of certain provisions under the Credit Facility Agreement. Under the Forbearance Agreement, Crystal agreed to forbear against any remedies available to them under an event of default until June 27, 2014. Crystal provided a waiver to the Company on June 27, 2014; as such, outstanding borrowings under the Credit Facility Agreement, as amended, was not callable as of the September 27, 2014 balance sheet date.

No other modifications were made pursuant to the Forbearance Agreement which materially impacted the terms of the Credit Facility Agreement dated February 6, 2014.

As of September 27, 2014, the Company had $12.0 million drawn against eligible accounts receivable, inventory and cash collateral and had no incremental borrowing capacity against its borrowing base collateral.

As of November 3, 2014, the Company had $4.5 million in cash and cash equivalents (excluding restricted cash), $12.0 million drawn against eligible accounts receivable, inventory and cash collateral and had no incremental borrowing capacity against its borrowing base collateral. Refer to Note 5. Debt herein for further disclosure regarding the Credit Facility Agreement and subsequent modifications and amendments.

- On June 27, 2014, the Company completed the previously announced review of financing, transactional and strategic alternatives with the closing of a private placement of $18.0 million in principal amount of its 7.5% subordinated secured convertible notes (the “Notes”). Interest on the notes will accrue at a stated rate of 7.5% per annum and each quarterly interest payment will be paid in kind by increasing the principal amount due under the notes unless the Company exercises its option to pay cash interest at a stated rate of 6.75% per annum. The Notes are convertible into shares of the Company’s common stock at any time at the option of the Noteholders at a conversion price of $3.50 per share (as adjusted for the Company's September 2014 reverse stock split), subject to certain adjustments. Refer to Note 5. Debt herein for further disclosure regarding the Notes.

Principles of Consolidation

In the opinion of management, the accompanying unaudited Condensed Consolidated Financial Statements include all adjustments, consisting primarily of normal and recurring adjustments, necessary for the fair presentation of consolidated financial position, results of operations, and cash flows for the interim periods presented. All intercompany accounts and transactions have been eliminated in consolidation. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). The fiscal year-end December 28, 2013 Consolidated Balance Sheet data was derived from audited financial statements, but does not include all disclosures required under GAAP. Accordingly, these unaudited Condensed Consolidated Financial Statements and related notes thereto should be read in conjunction with the consolidated financial statements and notes thereto for the fiscal year ended December 28, 2013, included in the Company’s Annual Report on Form 10-K, filed with the SEC.

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Fiscal Year
The Company’s fiscal year ends on the Saturday closest to December 31. As used herein, the interim periods presented are the thirteen week periods ended September 27, 2014 and September 28, 2013, respectively. The 2014 fiscal year ending January 3, 2015, includes 53 weeks of operations. The 2013 and 2012 fiscal years ended December 28, 2013 and December 29, 2012, respectively, included 52 weeks of operations.
Use of Estimates
The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. On an ongoing basis, management evaluates its estimates and assumptions, including those related to inventory valuation, property and equipment, recoverability of long-lived assets, including intangible assets, valuation of financial instruments, income taxes, and stock-based compensation.
Segment Reporting
The Financial Accounting Standards Board (“FASB”) has established guidance for reporting information about a company’s operating segments, including disclosures related to a company’s products and services, geographic areas and major customers. The Company has aggregated its net revenues generated from its retail stores and its direct business unit into one reportable segment. The Company aggregates its operating segments because they have a similar class of customer, nature of products, and distribution methods as well as similar economic characteristics. The Company has no international sales. All of the Company’s identifiable assets are in the United States.
Revenue Recognition
The Company recognizes revenue, and the related cost of goods sold, at point-of-sale or upon delivery to customers. Inventory shipping and handling fees billed to customers for online and catalog sales are included in net revenues, and the related shipping and handling costs are included in cost of goods sold. Based on historical sales returns, an allowance for sales returns is recorded as a reduction of net revenues in the periods in which the sales are recognized. Sales tax collected from customers is excluded from net revenues and is included as part of accrued expenses and other current liabilities on the unaudited Condensed Consolidated Balance Sheets.
The Company sells gift cards in its stores, which do not expire or lose value over periods of inactivity, and accounts for the gift cards by recognizing a liability at the time a gift card is sold. The Company recognizes income from gift cards and gift certificates when they are redeemed by the customer.
Income from unredeemed gift certificates and gift cards is recognized when it is determined that the likelihood of the gift certificate or gift card being redeemed is remote and when there is no legal obligation to remit unredeemed gift certificates and gift cards to relevant jurisdictions. Income from unredeemed gift certificates and gift cards is included in other income on the Company's unaudited Condensed Consolidated Statements of Comprehensive Loss.
Cash and Cash Equivalents
The Company considers all short-term investments with an initial maturity of three months or less when purchased to be cash equivalents. Included in the Company's cash equivalents are short term credit receivables.
Restricted Cash
The Company classifies certain cash balances as restricted when, in connection with its Credit Facility Agreement, the Company’s borrowing base collateral is less than $12 million.
Short-term Investments
The Company classifies its investments as available-for-sale. Short-term investments which have a maturity of one year or less at acquisition are carried at fair market value. Unrealized gains or losses, net of the related tax effect, are excluded from earnings and reported in accumulated other comprehensive income, a component of stockholders’ equity. A decline in the

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fair value of any available-for-sale security below cost that is deemed other than temporary results in a charge to earnings and the establishment of a new cost basis for the security. To determine whether the decline in fair value is other than temporary, the Company considers whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the decline in value, the severity and duration of the decline in value, changes in value subsequent to year-end and the forecasted performance of the investment. Interest income is recognized as earned. Income on investments includes the amortization of the premium and accretion of discount for debt securities acquired at other than par value. Realized investment gains and losses are determined on the basis of specific identification.

Debt Issuance Costs

Debt issuance costs are deferred and amortized over the contractual life of the underlying loan using the effective interest method when it is materially different than the straight-line method.

The Company had unamortized debt issuance costs of $1.2 million as of September 27, 2014 related to the debt agreement with Crystal dated February 6, 2014 and the subsequent First Amendment to Credit Agreement ("First Amendment") dated June 27, 2014. The Company had unamortized debt issuance costs of $1.6 million as of September 27, 2014 related to the issuance of $18.0 million in aggregate principal amount of its subordinated secured convertible notes. The short-term and long-term portions of the unamortized costs are included in prepaid expenses and other current assets, and in other assets, respectively.

The cash flow from deferred financing costs in year to date cash flow from financing includes an adjustment of approximately $900,000 that was previously included in cash flows from operations in the first quarter of 2014.

Modifications and Extinguishments

The Company accounts for modifications and extinguishments related to debt instruments in accordance with Accounting Standards Codification ("ASC") 470-50 Debt - Modifications and Extinguishments which provides guidance on whether an exchange of debt instruments with the same creditor constitutes an extinguishment and whether a modification of a debt instrument should be accounted for in the same manner as an extinguishment.

The Company accounts for debt transactions which are classified as modifications under the guidance by calculating a new effective interest rate based on the debt's carrying value and capitalizing and amortizing new costs paid to the creditor and expenses fees paid to third parties. Conversely, if the debt transaction is classified an extinguishment, the Company records a gain or loss for the difference between the carrying value of the original debt and the fair value of the new debt and both unamortized fees related to the extinguished debt, and previously capitalized fees paid to the creditor under the original debt are expensed.

Derivative Financial Instruments

The Company accounts for the call option of the convertible debt ("call option") and the written put option upon change in control associated with the subordinated secured convertible notes ("put option") (collectively the "derivative instruments") each as individual embedded derivative liabilities pursuant to ASC 815-15 Derivatives and Hedging - Embedded Derivatives. The derivative instruments are carried at fair value with changes in fair value recognized in earnings. The value of the embedded derivative is contingent upon changes in projections of future cash flows over the term of the debt. The resulting discount created by allocating a portion of the issuance proceeds to the embedded derivative is then amortized to interest expense over the term of the debt using the effective interest method. The Company determines the valuation of the derivative instruments at issuance and each reporting period end until such time as they are no longer required to be bifurcated.

Refer to Note 2. Financial Instruments for further disclosure regarding the significant inputs and assumptions considered in determining the estimated fair value of the derivative instruments. The call option is classified as a current liability on the Company's unaudited Condensed Consolidated Balance Sheets as it is exercisable upon demand from the note holders. The put option is classified as a long-term liability on the Company's unaudited Condensed Consolidated Balance Sheets. As of September 27, 2014, the Company has determined that there is no fair value associated with the put option upon change in control. The Company valued the put option at $0 with the assumption there is no material probability the Company will enter into a qualifying fundamental transaction during the three-year conversion term.

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Inventories

Inventories are comprised principally of women’s apparel and accessories and are stated at the lower of cost or market, on a first-in first-out basis, using the retail inventory method. Included in the carrying value of merchandise inventory, and reflected in cost of goods sold, is a reserve for shrinkage which is accrued between physical inventory dates as a percentage of sales based on historical inventory results.

The Company reviews its inventory levels to identify slow-moving merchandise and generally uses markdowns to clear this merchandise. The Company records a markdown reserve based on estimated future markdowns related to current inventory to clear slow-moving inventory. These markdowns may have an adverse impact on earnings, depending on the extent and amount of inventory affected. The markdown reserve is recorded as an increase to cost of goods sold in the unaudited Consolidated Statements of Comprehensive Loss.

Impairment of Depreciable Long-Lived Assets

The Company follows ASC 360, Property, Plant and Equipment, which requires impairment losses to be recorded on long-lived assets used in operations whenever events or changes in circumstances indicate that the net carrying amounts may not be recoverable. Long-lived asset groups are determined based on an assessment of the lowest level for which identifiable cash flows are independent of the cash flows of other groups of assets and liabilities. Examples of events or changes in circumstances are negative cash flows from operations, projected negative cash flow from operations associated with the use of an asset or asset group (collectively, the "Asset"), declines in market prices associated with an asset, etc. Once the Company has determined that a triggering event has occurred, and the intent is to hold the Asset for continued use, the Company performs an evaluation to compare whether the total undiscounted cash flows are greater or less than the Asset's carrying value ("recoverability test"). If the carrying value is greater than the undiscounted cash flows, the Company deems the Asset to be impaired. The cash flows used for determining the Asset's recoverability is subjective and requires significant judgment. The Company estimates the cash flows of its assets based on historical trends, internal budgets and projections, including sales, cost of goods sold, costs associated with repairs and maintenance, the primary asset's remaining useful life, expected salvage value, etc.

If the initial recoverability test indicates impairment, the Company uses an income valuation approach (discounted cash flows) to calculate the asset's fair value using the weighted-average cost of capital. To the extent that the carrying value exceeds the fair value, the Company recognizes an impairment loss, which would be included in income from operations.

During the third quarter of 2014, the Company determined that an impairment review of its stores' fixed assets was necessary based on continued negative comparable store trends and results of store operations underperforming against projections. The Company compared the undiscounted cash flows at the individual store level for recoverability and determined that 42 stores required analysis. In determining the discount factor to apply for assessing fair value, the Company used a discount rate of 26%, which approximates its weighted average cost of capital. Based on the results of management's assessment, the Company recognized a non-cash impairment loss related to its stores of $1.8 million during the third quarter of 2014, bringing the total impairment loss related to store fixed assets for the thirty-nine weeks ended September 27, 2014 to $3.7 million.

The Company is currently party to a lease between GIV Imeson, LLC and Body Central Stores, Inc. This lease term extends through August 31, 2021 for which the remaining lease payment obligation was $6.3 million as of September 27, 2014. During the fiscal third quarter of 2014, the Company terminated its plans to move to the corporate headquarters and distribution center at the One Imeson location. The Company is currently exploring alternatives to reduce, mitigate or terminate this obligation, although there can be no assurance that the Company will be able to do so on terms favorable to the Company. In accordance with ASC 360, Property, Plant and Equipment, the Company determined that there were impairment losses on long-lived assets that should be recorded. The Company incurred a $5.2 million non-cash charge during the third quarter of 2014 relating to the write down of all the remaining leasehold improvements associated with this property. The Company also wrote down the material handling equipment at this location to its appraised value of $1.1 million, thereby incurring a $2.0 million non-cash charge during the third quarter of 2014. The remaining material handling equipment at this location is classified as held for sale.

Goodwill and Other Intangible Assets

Goodwill and intangibles with indefinite lives are required by ASC 350-20 Intangibles - Goodwill and Other - Goodwill and ASC 350-30 Intangibles - Goodwill and Other - General Intangibles Other Than Goodwill to be tested for impairment annually. The Company conducts an impairment test of its recorded goodwill and other indefinite-lived intangible

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assets on the balance sheet date of each fiscal year, or more frequently if impairment indicators are present resulting from a change in circumstances. Pursuant to the guidance in ASC 350, the Company first performs a qualitative analysis of its trade name and of the goodwill of the stores and direct business reporting units to determine if a quantitative analysis is necessary. This analysis considers factors such as the year over year change in its competitive retail sector, comparable store sales, catalog and e-commerce sales, stock price fluctuations, actual and forecasted sales, the Company's market value relative to its book value, debt levels, and cash (used in) provided by operations. The qualitative analysis further evaluates the progress and impact of changes in its infrastructure and refinements to the Company’s strategic objectives. If, during the qualitative analysis, the Company determines that it is more likely than not that the carrying value of the reporting unit or trade name is greater than its fair value, a quantitative analysis is performed.

Goodwill and indefinite-lived intangible reviews are highly subjective and involve the use of significant estimates and assumptions. These estimates and assumptions can have a significant impact on the amount of any impairment loss recorded. The Company uses an income valuation approach (discounted cash flow) which is dependent on future sales trends, market conditions and the cash flows from each reporting unit over several years. Actual cash flows in the future may differ significantly from those previously forecasted. Forecasts consider the potential impact of certain factors including strategic growth initiatives centered on a more consistent and singular approach to branding, merchandise content and customer messaging, as well as expectations of improvements in comparable store sales trends. If these growth strategies are not achieved, the Company could experience a further impairment of intangible assets. Other significant assumptions in these forecasts include growth rates and the discount rates applicable to future cash flows.

The Company recorded impairment losses on its goodwill of $10.4 million in the second quarter of 2013 for its direct business reporting unit and $11.1 million during the fourth quarter 2013 for its stores reporting unit. Consequently, the Company has no remaining goodwill.

During the third quarter of 2014, the Company determined that a triggering event had occurred which required an analysis to determine whether an impairment loss should be recorded related to its trade name. In determining whether a triggering event had occurred, the Company considered the continued decline in its stock price, leading to its market capitalization falling below its net book value, and lower-than-expected sales for both the stores and direct reporting units. Based on these and other considerations, the Company concluded that a step 1 analysis of its trade name was necessary.

In performing step 1 of the impairment analysis, the Company applied the relief-from-royalty methodology (income approach pursuant to ASC 820 Fair Value). The Company estimated the required rate of return on its working capital and fixed assets by deducting the weighted, after-tax required returns on working capital, fixed assets, and other assets from the weighted average cost of capital. In order to estimate the royalty rate, the Company considered estimated long-term sales and margin growth, third-party royalty rate data, and the relative risk of the asset. The Company applied the estimated royalty rate to projected net sales, which was tax effected to estimate the after-tax royalty stream. The Company compared the $12.9 million carrying value of the trade name to the estimated fair value calculated using the relief-from-royalty discounted cash flow method and, based on the results of this analysis, the Company concluded that the carrying value of its trade name exceeded its fair value; as such, impairment of the Company's trade name was deemed necessary. The Company recorded an impairment loss of $5.1 million on its unaudited Condensed Consolidated Statements of Comprehensive Loss in the third quarter 2014.

Severance Costs

The Company accounts for severance costs pursuant to ASC 712 Compensation - Nonretirement Postemployment Benefits which requires employers that provide special or contractual termination benefits to recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated. The cost of termination benefits recognized as a liability and a loss includes the amount of any lump-sum payments and the present value of any expected future payments.

Reclassifications

The Company reclassified interest expense and interest income to reflect the gross presentation for the thirteen weeks and thirty-nine weeks ended September 28, 2013 to conform to the presentation for the thirteen weeks and thirty-nine weeks ended September 27, 2014. The Company also reclassified income taxes receivable out of prepaid expense as of September 28, 2013 and December 28, 2013 to conform to the presentation as of September 27, 2014.

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Recently Issued Accounting Standards

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers. ASU No. 2014-09 requires entities to perform a five step process which is using to determine the timing of revenue recognition. The guidance establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity’s contracts with customers. The core principle of this guidance is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in ASU No. 2014-09 are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early adoption of the guidance is not permitted. The Company is in the process of evaluating the impact of the guidance to determine if adoption will materially impact the Company's financial statements or disclosures.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern. The guidance is intended to define management’s responsibility to evaluate whether there is substantial doubt about an organization’s ability to continue as a going concern and to provide related footnote disclosures. Under GAAP, financial statements are prepared under the presumption that the reporting organization will continue to operate as a going concern, except in limited circumstances. Financial reporting under this presumption is commonly referred to as the going concern basis of accounting. The going concern basis of accounting is critical to financial reporting because it establishes the fundamental basis for measuring and classifying assets and liabilities. The amendments in ASU No. 2014-15 are effective in the annual period ending after December 15, 2016. Early adoption of the guidance is permitted. The Company is in the process of evaluating the impact of the guidance to determine if adoption will materially impact the Company's financial statements or disclosures.

2. Financial Instruments

The FASB-issued guidance establishes a framework for measuring fair value that is based on the inputs market participants use to determine fair value of an asset or liability and establishes a fair value hierarchy to prioritize those inputs. The guidance under this statement describes a hierarchy of three levels of input that may be used to measure fair value:

- Level 1 — Inputs based on quoted prices in active markets for identical assets and liabilities.
- Level 2 — Inputs other than Level 1 quoted prices, such as quoted prices for similar assets and liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.
- Level 3 — Unobservable inputs based on little market or no market activity and which are significant to the fair value of the assets and liabilities.

The Company’s material financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, debt, and derivative instruments. The fair values of cash, accounts receivable, accounts payable and accrued expenses approximate their carrying values based on their short-term nature. Considerable judgment is required in interpreting market data to develop estimates of fair value. The fair value estimates presented herein are not necessarily indicative of the amount that the Company or the debt holders could realize in a current market exchange. The use of different assumptions and/or estimation methodologies may have a material effect on the estimated fair value.

Money market securities and tax-free municipal bonds with an initial maturity date of three months or less when purchased are classified as cash and cash equivalents on the accompanying unaudited Condensed Consolidated Balance Sheets. Municipal bonds with an initial maturity date greater than three months when purchased and a maturity of one year or less are classified as short-term investments on the accompanying unaudited Condensed Consolidated Balance Sheets.

On June 27, 2014, the Company entered into a convertible debt agreement which included an embedded derivative written call option related to the conversion of the Notes into shares of common stock (the "call option") and an embedded put option ("put option") related to a fundamental transaction or change of control provision (collectively, the "derivative instruments"). Under the provisions in ASC 815 Derivatives and Hedging, the embedded derivatives are required to be accounted for separately from the debt instrument as liabilities. Such bifurcation requires the embedded derivatives to be recorded at their inception fair value. On a go-forward basis, the embedded derivatives are required to be marked-to-market

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with the impact of any change in fair value recorded as a (gain) loss on the Company's (un)audited Statements of Comprehensive Gain/(Loss).

The Company valued the put option at $0 with the assumption there is no material probability the Company will enter into a qualifying fundamental transaction during the three-year conversion term.

The Company valued the call option using a modified binomial lattice solution whereby the Notes were valued with and without the conversion feature and the difference was attributed to the call option. The fair value of the call option was calculated with the following assumptions:

Valuation Inputs	September 27, 2014	
Market value of common stock on measurement date (1)	$1.95	
Adjusted conversion price (2)	$3.50	
Risk free interest rate (3)	0.95	%
Credit-Adjusted Discount Rate (4)	40	%
Life of the note in years	2.75	
Expected volatility (5)	100	%
Expected dividend yield (6)	0.0%	

(1)The market value of common stock is based on the closing market price as of September 26, 2014.

(2) The adjusted conversion price is calculated based on conversion terms described in the note agreement and adjusted for the Company's 1-for-10 reverse stock split.

(3) The risk-free interest rate was determined using an interpolated 2.75 year Treasury Bill rate

(4) The credit-adjusted discount rate was developed from yields on comparable debt instruments.

(5) The volatility factor was estimated by management using the historical volatilities of the Company’s stock.

(6) Management determined the dividend yield to be 0% based upon its expectation that it will not pay dividends for the foreseeable future.

The embedded derivatives are classified as Level 3 in the hierarchy. Refer to Note 6. Derivative Financial Instruments for further disclosure related to the embedded derivatives.

Description	September 27, 2014 (in thousands)	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Derivative Instruments				
Call Option	$6,925	$—	$—	$6,925
Put Option	—	—	—	—
Total	$6,925	$—	$—	$6,925

The fair value of the call option derivative at June 28, 2014 was $13.2 million. The most significant factor in the decrease from June 28, 2014 to September 27, 2014 was the drop in share price (adjusted for the 1-for-10 reverse stock split) from $10.00 to $1.95. Another factor is the change in the remaining life from 3.00 to 2.75 years.

In addition to the derivative instruments, the convertible notes payable had an estimated fair value of $7.9 million as of September 27, 2014.

The Company has determined the estimated fair value amounts of its financial instruments using available market information for those financial instruments that are measured at fair value on a recurring basis. As of September 28, 2013, the Company held the following:

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Description	September 28, 2013 (in thousands)	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Municipal Bonds	$5,022	$—	$5,022	$—
Total	$5,022	$—	$5,022	$—

As of September 28, 2013, municipal bonds in the amount of $0.7 million were included in cash and cash equivalents.

3. Income Taxes

The provision for income taxes is based on the current estimate of the annual effective tax rate and is adjusted as necessary for discrete events occurring in a particular period. The effective income tax rate was 12.5% and 43.0% for the thirteen weeks ended September 27, 2014 and September 28, 2013, respectively, and 7.5% and 26.8% for the thirty-nine weeks ended September 27, 2014 and September 28, 2013, respectively. The decrease for the thirteen weeks ended September 27, 2014 as compared to the thirteen weeks ended September 28, 2013 was primarily due to a $4.9 million increase in the valuation allowance recorded by the Company against its deferred tax asset. Recent or future changes in equity ownership could result in limitations to the Company's ability to carryforward Net Operating Losses to future periods. As of September 27, 2014, the valuation allowance against the Company's deferred tax asset was $18.8 million.

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	September 27, 2014	September 28, 2013	September 27, 2014	September 28, 2013
Amount computed using statutory rates	35.0 %	35.0 %	35.0 %	35.0 %
State and local income taxes, net of federal benefit	4.2	3.8	4.0	2.7
Impairment of goodwill	—	—	—	(14.3)
Change in valuation allowance	(26.5)	—	(31.3)	—
Other	(0.2)	4.2	(0.2)	3.4
Provision for income tax rate	12.5 %	43.0 %	7.5 %	26.8 %

The Company recognizes income tax liabilities related to unrecognized tax benefits in accordance with FASB ASC 740, Income Taxes, guidance related to uncertain tax positions, and adjusts these liabilities when they change as the result of the evaluation of new information. The Company has no material uncertain tax positions which would result in a related income tax liability as of September 27, 2014.

4. Leases

Operating Leases

The Company’s retail stores and corporate offices are in leased facilities. Lease terms for retail stores generally range up to ten years and provide for escalations in base rents. The Company does not have obligations to renew the leases. Certain leases provide for contingent rentals based upon sales. Most leases also require additional payments covering real estate taxes, common area costs and insurance.

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Future minimum rental commitments, by year and in the aggregate, under non-cancelable operating leases as of September 27, 2014, are as follows:

Fiscal Year	(in thousands)
2014 remaining	$6,476
2015	23,412
2016	20,773
2017	16,623
2018	11,274
Thereafter	14,618
Total	$93,176

Sale-Leaseback Agreement

On November 12, 2013, the Company entered into a sale-leaseback arrangement to finance its information technology initiatives. Under the agreement, the Company is leasing back the property and equipment from the buyer/lessor over a period of four years, upon which, the Company intends to exercise the bargain purchase option to repurchase the property and equipment. The transaction has been accounted for as a financing arrangement, wherein the property remains on the Company's unaudited Condensed Consolidated Balance Sheets and will continue to be depreciated over the assets' useful lives. A financing obligation, net of repayments, in the amount of $2.5 million was recorded under "Financing obligation, sale leaseback" on the Company's unaudited Condensed Consolidated Balance Sheets and is being reduced based on the payments under the lease. The minimum annual rental payments are as follows:

Fiscal Year	(in thousands)
2014 remaining	$222
2015	887
2016	887
2017	739
Total minimum payments	$2,735
Amounts representing interest	230
Financing obligation, sale-leaseback	$2,505

5. Debt

Notes payable and long-term debt consists of:

	September 27, 2014	December 28, 2013
	(in thousands)	
1.35% + one month LIBOR Revolving Line of Credit - settled February 6, 2014	$—	$5,000
8% + 90-day LIBOR Senior Credit Facility - $17.0 million revolving line of credit due February 6, 2017	12,000	—
7.5% Subordinated Convertible Notes due June 27, 2017	5,589	
Amount due after one year	$17,589	$5,000

Fully Settled Revolving Credit Facility

On January 20, 2012, the Company entered into a Line of Credit Agreement with Branch Banking and Trust Company ("BB&T") that provided for a revolving line of credit facility in the amount of $5.0 million with an accordion feature that allowed BB&T to increase the facility up to $20.0 million at its sole discretion. The facility had an original maturity date of May 5, 2013. The facility bore interest at the one month LIBOR rate plus 1.35% per annum, as adjusted monthly on the first day of each month, with an all-in floor rate of 2.0%. The facility was secured by all the assets of the Company. The Line of Credit Agreement included a financial covenant requiring the Company to have a Tangible Net Worth (as defined in the Line of Credit Agreement) of $30.0 million quarterly, and other customary covenants.

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On March 8, 2013, the Company renewed the Line of Credit Agreement; the renewed facility had a maturity date of March 5, 2015. There were no significant changes to the terms or conditions from the original agreement dated January 20, 2012.

On February 6, 2014, the Company repaid the $5.0 million outstanding under its Branch Banking and Trust Company revolving Line of Credit and closed the credit facility.

Senior Credit Facility

On February 6, 2014, the Company entered into a new asset based credit facility agreement (the "Credit Facility Agreement") with Crystal, as administrative and collateral agent.

The Credit Facility Agreement provided for a $17.0 million senior secured credit facility, which included a term loan facility of $12.0 million advanced on the closing date and a revolving credit facility of $5.0 million that was not drawn upon on the closing date. Additionally the Credit Facility Agreement provided for an uncommitted term loan facility of up to $7.0 million. The Credit Facility Agreement will mature on February 6, 2017 and is secured by substantially all of the Company's assets. The proceeds of the term loan facility were used to pay all amounts owed under its prior $5.0 million revolving credit facility with Branch Banking and Trust Company, to pay certain related fees and expenses, to fund working capital and for other corporate purposes. The Company is required to pay interest only on the term loan facility until the maturity date, at which time borrowings under the term loan facility become due in full. Borrowings under the Credit Facility Agreement bear interest at the 90-day LIBOR rate plus 8.0%. The continued availability of advances under the term loan facility and the amounts committed under the revolving facility were subject to maintenance of specified borrowing base requirements. The borrowing base was calculated as 100% of the net orderly liquidation value ("NOLV") of eligible inventory plus 95% of eligible receivables and cash in blocked accounts, plus 50% of the NOLV of eligible equipment less availability reserves and a $3.0 million availability block. The Company is subject to an unused facility fee of 0.50% on the unused portion of the revolving facility and the unused portion of the $5.0 million commitment in excess of the revolver. An early termination fee of the greater of a make-whole amount and 3.00% applied if the term loan facility was prepaid or if the commitments under the revolving facility were permanently reduced within the first year; a 2.00% fee would be applicable if such a prepayment or permanent reduction occurred during the second year. There was no such fee payable after the second year.

The Credit Facility Agreement included terms and conditions for cash dominion events which would be triggered by any of the following: (1) the occurrence and continuance of any event of default, (2) outstanding borrowings under the revolving credit facility, or (3) a failure by the Company to maintain unrestricted cash in an amount of at least $6.5 million for three consecutive business days or $3.5 million at any time.

The Credit Facility Agreement included standard terms and conditions, limitations and specified exclusions with regard to the Company's ability to, among other things: incur debt and contingent obligations; create liens; sell, transfer, license, lease or otherwise dispose of property; expand or contract their retail operations beyond certain specified levels; make investments, loans and advances; engage in certain mergers and consolidations; issue equity securities; engage in speculative transactions; make distributions and dividends; and engage in transactions with affiliates. There were no financial covenants under the Credit Facility Agreement.

The Credit Facility Agreement contained standard terms and conditions related to events of default, which were subject to specific thresholds and, in certain cases, cure periods. If an event of default occurred and continued under the Credit Facility Agreement, Crystal may, among other things, terminate their obligations to lend under the Credit Facility Agreement and require the Company to repay all amounts owed under the credit facilities.

In connection with the June 23, 2014 Forbearance and Modification Agreement, the Company acknowledged certain defaults under the Credit Facility Agreement which triggered a cash dominion event and an accelerated borrowing base event. The parties agreed to forbear certain remedies to such defaults for a specified time frame as more fully discussed below.

On September 2, 2014, cash dominion was triggered as a result of our unrestricted cash falling below $7.5 million for two consecutive business days. As a result, until such time as our unrestricted cash exceeds $7.5 million for 60 consecutive calendar days, as to which there can be no assurance, inbound cash receipts will be controlled by Crystal. As the cash dominion event is not considered an Event of Default under the Credit Facility Agreement, the Company will continue to be allowed to borrow thereunder, subject to the other terms and conditions of the Credit Facility Agreement. Any acceleration of any of the

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Company's outstanding indebtedness would materially and adversely affect its business, and could affect its ability to continue as a going concern. The Company remained in dominion as of November 6, 2014.

Forbearance and Modification Agreement

On June 23, 2014, the Company entered into a forbearance and modification agreement (the “Forbearance Agreement”) with several lenders (the “Lenders”) and Crystal under the Credit Facility Agreement, dated as of February 6, 2014. The Forbearance Agreement amended the Credit Facility Agreement to, among other things, exclude certain representations as conditions precedent to borrowing until June 27, 2014 (together, with the Forbearance Effective Date, the “Forbearance Period”) with regard to certain events of default under the Credit Facility Agreement so long as the Company complied with the terms of the Forbearance Agreement.

On June 23, 2014 (the "Forbearance Effective Date"), the Company’s revolving line of credit increased from $5.0 million to $17.0 million and the Company fully prepaid its $12.0 million term loan in cash.

As of the Forbearance Effective Date, the Company was in default of certain provisions of the Credit Facility Agreement, primarily for failure to pay certain obligations timely and the Company's actions undertaken to suspend the operation of the business in the ordinary course. These events of default triggered a Borrowing Base Acceleration Event and a Cash Dominion Event. Under the terms of the Forbearance Agreement, Crystal agreed to forbear from exercising their rights and remedies from the Forbearance Effective Date until June 27, 2014. These conditions required the Company to, among other things, (i) discharge every obligation and covenant performed under the Credit Facility Agreement, (ii) refrain from paying any subordinated indebtedness, (iii) take certain actions to comply with lease agreements, and (iv) to timely pay rent and/or other amounts due under the lease agreement for its current corporate headquarters and distribution center.

In connection with the payment of the $12.0 million outstanding on the term loan and contemporaneous $12.0 million increase in the revolving facility, the Company evaluated the transaction to determine whether the exchange should be accounted for as a modification or extinguishment under the provisions of ASC 470-50, which allows for an exchange of debt instruments between the same debtor and creditor to be accounted for as a modification so long as the instruments do not have substantially different terms. The guidance considers a transaction to have "substantially different terms" when the difference in the present value of the cash flows under the terms of the new debt instrument is at least 10 percent different from the present value of the remaining cash flows under the terms of the original instrument. The Company determined that the transaction did not meet the definition of "substantially different terms" and therefore accounted for the transaction as a modification.

Waiver and First Amendment to Credit Agreement

On June 27, 2014, the Company entered into the Waiver and First Amendment to Credit Agreement ("First Amendment") with Crystal. Amendments to the Credit Facility Agreement included, among other things, (i) the addition of clarifying language to certain definitions; (ii) clarification as to the allowable amount of eligible in-transit inventory (i.e., inventory in-transit cannot exceed 15% of eligible inventory and $750,000) and eligible equipment used to calculate the borrowing base; (iii) modification of the triggering conditions for a cash dominion event from a failure by the Company to maintain unrestricted cash in an amount of at least $6.5 million for three consecutive business days or $3.5 million at any time, to a failure by the Company to maintain unrestricted cash of $7.5 million for two consecutive business days; (iv) the calculation of the early termination fee based on the period in which the prepayment or termination occurs; and (v) to incorporate the Company's newly issued Subordinated Secured Convertible Notes (as discussed in detail below). Additionally, the First Amendment, although the conditions of default were continuing, Crystal provided a waiver whereby any cash dominion event existing prior to the First Amendment date, were terminated and provided Crystal's intent to terminate and/or rescind instructions to any blocked bank account it sent while the Company was in cash dominion.

As of September 27, 2014, the Company had $12.0 million drawn against eligible accounts receivable, inventory and cash collateral and had no incremental borrowing capacity against its borrowing base collateral.

As of November 3, 2014, the Company had $4.5 million in cash and cash equivalents (excluding restricted cash), $12.0 million drawn against eligible accounts receivable, inventory and cash collateral and had no incremental borrowing capacity against its borrowing base collateral. Refer to Note 5. Debt herein for further disclosure regarding the Credit Facility Agreement and subsequent modifications and amendments.

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Subordinated Secured Convertible Notes

Effective as of June 27, 2014, the Company entered into a securities purchase agreement (the “Purchase Agreement”) with investors (the “Noteholders” or "Buyers") and closed the issuance and sale of $18.0 million in aggregate principal amount of its subordinated secured convertible notes (the “Notes”) and two new series of preferred stock (the “Preferred Stock”). The Notes are guaranteed by the Company and its subsidiaries have a second lien against the Company’s assets, and are junior only to liens of senior debt and certain permitted liens. All amounts under the Notes will be due and payable in cash on the maturity date, June 27, 2017, if not converted or redeemed earlier. As discussed in Note 2. Financial Instruments, the Notes contain an embedded call option related to the conversion of the Notes into shares of the Company's common stock and an embedded put option related to a fundamental transaction or change in control which is fair valued with the residual value becoming the fair value of the debt. As such, the fair value of the Notes is less than the aggregated principal amount of $18.0 million. Both the Credit Facility Agreement and the Notes contain customary representations, warranties, and cross-default provisions with respect to other material indebtedness.

Description of Notes

The Notes are convertible into shares of the Company’s common stock, par value $0.001 per share, at any time, in whole or in part, at the option of the Noteholders at a fixed conversion price, initially set at $3.50 per share (as adjusted for the Company's September 2014 reverse stock split), which is subject to adjustment for stock splits, combinations or similar events and subsequent dilutive issuances during the term of the Notes. Limitations on conversions are such that no Noteholder can beneficially own in excess of 9.99% of the shares of the Company's common stock outstanding immediately after conversion and/or, should there not be sufficient shares available, conversions will be made on a pro rata basis based on principal requests for conversion. The Noteholder can continue to convert their Notes into shares of the Company's common stock until all security interest in the Notes have been exercised or until the Notes have matured and any principal and accrued interest outstanding has been settled. Total shares into which the Notes can be converted as of the balance sheet date is 5,142,864.

Interest on the Notes is due on the first day of each calendar quarter and will either (i) accrue and capitalize interest at the stated rate of 7.5% per annum which will be added to the outstanding principal or (ii) at the election of the Company and subject to the terms of the Subordination Agreement, the Company may make cash payments of the quarterly interest amounts at the discounted stated rate of 6.75% per annum. A default interest rate of 20% would apply upon the occurrence and continuance of an event of default. A late charge of 20% of any overdue amount will apply if the Company fails to pay amounts due under the Notes when due.

The Notes contain certain covenants and restrictions and are subject to various events of default, including, among others, failure to effect a reverse stock split of at least 1-for-10 within 90 days (which split was implemented by the Company in September 2014); failure to pay principal or stated interest on the Notes within 7 days of the due date; failure by the Company to file, or for the SEC to declare effective, the registration statement covering the resale of the underlying shares within contractually accepted time periods; suspension from trading on an eligible market; failure to deliver the required number of shares pursuant to a conversion within 30 days of the conversion date; a failure by the Company to pay its debts as they become due in the ordinary course of business; or to comply with other certain covenants under the Notes and cross-defaults to other material indebtedness.

After certain senior indebtedness related to the Crystal agreement, as amended, and the Company's sale-leaseback financing agreement has been paid in full, the Notes contain events of default for failure by the Company to comply with its obligations to reserve common stock for any conversions of the Notes, convert the Notes or register for resale the common stock issuable upon such conversion. Upon a change of control of the Company, the Noteholders may require the Company to redeem the Notes for cash at a redemption price equal to the greater of (i) 107.5% of the principal amount of the Notes being redeemed plus any make whole amount (i.e., the interest that would have been paid through the maturity date had the change in control not occurred) or (ii) the product of the sum of (A) the conversion amount being redeemed and (B) the make whole amount and (y) the quotient determined by dividing (A) the cash amount per share of common stock which the Holder would have been entitled to receive upon the occurrence of such change in control had the Notes been converted immediately prior to such change in control by (B) the lowest conversion price in effect during the period beginning on the date immediately preceding the earlier of the change in control and the announcement to the public of the change in control and ending on the date the Holder

delivers the change in control redemption notice.
The Agreements also include a down round provision whereby, upon the issuance of other securities for a consideration per share which is less than the conversion price, the conversion price will be reduced to an amount equal to the new issuance price. Included in this provision are adjustments resulting from issuances of options, issuances of other

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convertible securities, changes in option prices or rate of conversion, adjustments to conversion price upon subdivision or combinations of common stock, and other voluntary adjustments.

The Company has accounted for the $18.0 million Notes in accordance with ASC 470-20 Debt with Conversion and Other Options as a single financial instrument as a non-current liability. In accordance with ASC 815, the Company is required to bifurcate the call and put options ("derivative instruments") from the debt host instrument. The Company derived the initial fair value of the derivative to be $13.2 million. This resulted in an unamortized discount on the value of the debt of $13.2 million, thereby valuing the initial debt component to be value of $4.8 million. The derivative instrument is marked to market, with the change recorded to earnings. The initial debt value is amortized through the maturity date using the effective interest method.

Registration Requirements

In connection with the Purchase Agreement, the Company entered into a Registration Rights Agreement (as amended, the "Registration Agreement") with the Buyers providing for the registration for resale of the shares of common stock issuable upon conversion of the Notes. Under the Registration Agreement, the Company was obligated to file a registration statement within 20 calendar days from the date the reverse stock split attained stockholder approval and to use its reasonable best efforts to cause the registration statement to become effective within 90 calendar days from the date the registration statement is filed and maintain the effectiveness of such registration statement until all of the shares registered thereunder may be freely transferred by the Buyers or the Buyers have sold all of the shares covered by such registration statement. In the event that the registration statement does not cover all of the Registrable Securities, the Company will be obligated to file additional registration statements. The Company filed a Form S-1 Registration Statement with respect to the registrable securities on September 24, 2014, which registration statement has not yet been declared effective by the Commission.

The Company will be subject to certain obligations if the Company (i) fails to file the registration statement within the agreed upon time period; (ii) fails to have the registration statement declared effective on or before the agreed upon date; or (iii) fails to maintain the effectiveness of the registration statement or fails to meet certain other maintenance obligations. If the Company fails to meet these obligations, subject to the terms of the Intercreditor and Subordination Agreement defining the rights as between the Company's senior secured credit facility lenders and the Noteholders, it will be required to pay liquidated damages equal to 2% of the purchase price of the registrable securities relating to such registration statement upon the occurrence of the failure and for each 30 calendar day period during which such failure is continuing, with liquidation damages being capped at 15% of the aggregated purchase price of the registrable securities.

First Amendment to the Securities Purchase Agreement, Notes and Registration Rights Agreement

On July 15, 2014, the Company entered into a First Amendment to Securities Purchase Agreement, Notes, and Registration Rights Agreement (the "Amendment") with the Noteholders which effects certain modifications to the Purchase Agreement, Subordinated Secured Convertible Notes, and the Registration Rights Agreement (collectively, the "Agreements") entered into on June 27, 2014. The Amendment amended certain covenants contained in the Agreements to provide for the following: (i) the definition of "Eligible Market" was amended to include, among others, the OTC Pink or any other comparable OTC market; (ii) the definition of "Initial Filing Deadline" for filing the initial registration statement covering the resale of the shares issuable upon conversion of the Notes was amended to mean the date which is 20 calendar days after the Company has obtained stockholder approval of the1-to-10 reverse stock split pursuant to the Securities Purchase Agreement; and (iii) to include language that eliminates the penalty fee provision associated with any failure by the Company to timely register the required number of shares provided that the number of shares available under the Registration Statement is sufficient to cover the lesser of (1) at least 100% of the maximum amount of conversion shares or (2) the lesser of the maximum number of shares of common stock of the Company permitted to be registered by the SEC or authorized pursuant to the Company's Certificate of Incorporation.

6. Derivative Financial Instruments

Convertible Option

The fair value of the embedded derivative call option related to the convertible debt was $6.9 million as of September 27, 2014. The Company recognized a gain of $6.3 million during the third quarter of 2014 for the change in the fair value of the call option.

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Refer to Note 2. Financial Instruments to the Company's unaudited Notes to the Condensed Consolidated Financial Statements for information about the valuation techniques and assumptions the Company uses to measure the fair value of its embedded derivative call option related to the convertible debt.

Put Option upon Change in Control

The Company determined that embedded derivative put option related to the convertible debt had no fair value as of September 27, 2014, resulting from the Company's assessment of improbability of occurrence. The Company has not recognized a gain or loss for the change in the fair value of the put option in its unaudited Condensed Consolidated Financial Statements. Refer to Note 2. Financial Instruments to the Company's unaudited Notes to the Condensed Consolidated Financial Statements for information about the valuation techniques and assumptions the Company uses to measure the fair value of its embedded derivative put option related to the convertible debt.

7. Equity Incentive Plans and Employee Stock Purchase Plan

On May 14, 2014, the Company's shareholders approved an amendment and restatement of the 2006 Equity Incentive Plan (the "2006 Plan") in the form of the Amended and Restated 2006 Equity Incentive Plan ("Restated Plan"). The Restated Plan replaces the 2006 Plan. The Restated Plan provides flexibility to the compensation committee to use various equity-based incentive awards as compensation tools to motivate the Company’s workforce. The Restated Plan will expire on May 14, 2024.

Under the Restated Plan: (i) the maximum number of shares of common stock to be issued under the Restated Plan is 500,000 shares in addition to those shares previously authorized and available under the 2006 Plan to be issued and (ii) shares tendered or held back for taxes will not be added back to the reserved pool under the Restated Plan. Upon the exercise of a stock appreciation right, the full number of shares underlying the Award will be charged to the reserved pool. Additionally, shares reacquired by the Company on the open market or otherwise using cash proceeds of option exercises will not be added to the reserved pool; (iii) the award of stock options (both incentive and non-qualified options), stock appreciation rights, restricted stock, restricted stock units, unrestricted stock, performance shares, dividend equivalent rights and cash-based awards is permitted; (iv) minimum vesting periods are required for grants of restricted stock, restricted stock units and performance share awards; (v) without stockholder approval, the exercise price of previously issued stock options and stock appreciation rights will not be reduced, and stock options and stock appreciation rights will not be otherwise repriced through cancellation in exchange for cash, other awards or stock options or stock appreciation rights with a lower exercise price; and (vi) any material amendment to the Restated Plan is subject to approval by our stockholders.

At the 2014 Special Meeting of Stockholders of the Company held on September 4, 2014, the Company’s stockholders duly approved the Body Central Corp. Third Amended and Restated 2006 Equity Incentive Plan (the “Amended and Restated Equity Plan”), which amends and restates the Restated Plan. As a result of the adoption of the Amended and Restated Equity Plan, key changes to the Restated Plan include the following:

- an increase by 630,000 in the number shares of common stock available for issuance;
- the maximum number of stock options or stock appreciation rights that may be granted to any one individual during any one calendar year period will be 1,500,000 shares, and if any award of restricted stock, restricted stock units or performance shares granted to an individual is intended to qualify as “performance-based compensation” under Section 162(m) of the Code, then the maximum award shall not exceed 3,000,000 shares;
- elimination of the ability to grant dividend equivalent rights, except in connection with the awards of restricted stock units; and
- awards of restricted shares and restricted stock units subject to a time-based vesting restriction may have a total vesting period less than three years.

Pursuant to the Employment Agreement, entered into on August 1, 2014 and effective as of June 30, 2014, by and between Body Central Corp. and Richard L. Walters, Jr., the Company is obligated to provide Mr. Walters certain monetary and equity compensation. The equity compensation contemplated in Mr. Walters agreement has not yet been issued and is expected to be issued subject to the refinement of the related award documentation. The awards contemplated in Mr. Walters employment agreement are anticipated to vest based on time parameters and performance criteria. The awards are as follows:

(i) a grant of 65,750 shares of the Company's restricted common stock, subject to time-based vesting in annual installments

(ii) three performance-based stock awards, each consisting of 65,750 shares of the Company's restricted common stock, and providing for vesting in the event the Company achieves certain performance targets as follows: (a) as to the first performance-based award, upon the successful completion of four consecutive quarters of positive cash flow,

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(b) as to the second performance-based award, upon the achievement by the Company of free cash flow equivalent to $20 million of EBITDA and (c) as to the third performance-based award, upon the achievement by the Company of free cash flow equivalent to $40 million of EBITDA.

On September 4, 2014, the Body Central Corp. 2014 Employee Stock Purchase Plan (the “ESPP”) was duly approved by the Company’s stockholders. The ESPP, provides for among other things, that participants may purchase the Company's stock at a 15% discount to the fair market value (as calculated in accordance with the ESPP) subject to certain plan provisions and discretion of the board of directors. An aggregate of up to 150,000 shares are authorized for sale pursuant to the ESPP.

Stock-based compensation expense of $200,000 and $790,000, net of forfeitures, for the thirteen weeks ended September 27, 2014 and September 28, 2013, respectively, are included in selling, general and administrative expenses and $(40,000) and $174,000, net of forfeitures, for the thirteen weeks ended September 27, 2014 and September 28, 2013, respectively, is included in cost of goods sold on the Company’s unaudited Condensed Consolidated Statements of Comprehensive Loss.

Stock-based compensation expense of $710,000 and $2.2 million, net of forfeitures, for the thirty-nine weeks ended September 27, 2014 and September 28, 2013, respectively, are included in selling, general and administrative expenses and $(89,000) and $(109,000), net of forfeitures, for the thirty-nine weeks ended September 27, 2014 and September 28, 2013, respectively, are included in cost of goods sold on the Company’s unaudited Condensed Consolidated Statements of Comprehensive Loss. The Company did not capitalize any expense related to stock-based compensation.

Option Awards

The fair value of each option grant for the thirty-nine weeks ended September 27, 2014 and September&#1