INNOVO GROUP INC
Form 10-K/A
February 09, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 1 to

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the fiscal year ended November 25, 2006

Commission file number: 0-18926

INNOVO GROUP INC.

(Exact name of registrant as specified in its charter)

Delaware	**11-2928178**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

5901 South Eastern Avenue, Commerce, California 90040
(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code: **(323) 837-3700**

Securities registered pursuant to Section 12 (b) of the Act:
Common Stock, $0.10 par value
(Title of Class)

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

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

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

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant based on the closing price of the registrant s common stock on The Nasdaq Stock Market, Inc. as of May 26, 2006, was approximately $19,254,000.

The number of shares of the registrant s common stock outstanding as of February 8, 2006 was 41,177,801.

Documents incorporated by reference: Portions of the registrant s definitive proxy statement to be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year are incorporated by reference in Part III of this Annual Report on Form 10-K.

Explanatory Note

This Amendment No. 1 on Form 10-K/A is being filed by Innovo Group Inc. to amend our Annual Report on Form 10-K for the fiscal year ended November 25, 2006 filed with the Securities and Exchange Commission on February 8, 2007, or the Initial Report. This Amendment No. 1 is being filed for the sole purpose of correcting a typographical error on our Consolidated Statement of Cash Flows on the Accounts Receivable line for the year ended November 26, 2005.

Our Consolidated Statement of Cash Flows in the Initial Report inadvertently reported the Changes in operating assets and liabilities: Accounts receivable for the year ended November 26, 2005 as the number 263 instead of the correct number 2,631 for such period.

This report speaks as of the original filing date, and except as indicated, has not been updated to reflect events occurring subsequent to the original filing date.

INNOVO GROUP INC.

FORM 10-K ANNUAL REPORT

FOR THE FISCAL YEAR ENDED NOVEMBER 25, 2006

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PART I

Forward-Looking Statements

Statements contained in this Annual Report on Form 10-K, or Annual Report, and in future filings with the Securities and Exchange Commission, or the SEC, in our press releases or in our other public or shareholder communications that are not purely historical facts are forward-looking statements. Statements looking forward in time are included in this Annual Report pursuant to the safe harbor provision of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements include, without limitation, any statement that may predict, forecast, indicate, or imply future results, performance, or achievements, and may contain the words, believe , anticipate , expect , estimate , inte plan , project , will be , will continue , will likely result , and any variations of such words with similar meanings. These statements are not guarantees of future performance and are subject to certain risks and uncertainties that are difficult to predict; therefore, actual results may differ materially from those expressed or forecasted in any such forward-looking statements.

Factors that would cause or contribute to such differences include, but are not limited to, the risk factors contained or referenced under the headings Business, Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations set forth in this Annual Report. In particular, certain risks and uncertainties that we face include, but are not limited to, risks associated with:

- our ability and success in implementing our strategic plan to focus our resources on our Joe s® brand;
- our ability to operate profitably and effectively manage expenses;
- our ability to execute and successfully implement a proposed merger with JD Holdings Inc., the successor-in-interest to JD Design LLC from whom we have our Joe s® license;
- our ability to maintain requirements to list our common stock on Nasdaq;
- our reliance on our Joe s® brand to generate revenue; and
- our ability to maintain and effectively manage relationships with vendors and third parties to whom we outsource certain of our business operations.

Since we operate in a rapidly changing environment, new risk factors can arise and it is not possible for our management to predict all such risk factors, nor can it assess the impact of all such risk factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, readers are cautioned not to place undue reliance on forward-looking statements that only speak as of the date of this filing.

We undertake no obligation to publicly revise these forward-looking statements to reflect events, circumstances or the occurrence of unanticipated events that occur subsequent to the date of this Annual Report. As used in this Annual Report, the terms we , us , our , and Innovo Group refer to Innovo Group Inc. and our subsidiaries and affiliates, unless the context indicates otherwise.

ITEM 1. BUSINESS

Overview

We began our operations in April 1987 as Innovo, Inc., or Innovo, a Texas corporation, to manufacture and domestically distribute cut and sewn canvas and nylon consumer products for the utility, craft, sports licensed and advertising specialty markets. In 1990, Innovo merged into Elorac Corporation, a Delaware corporation, and renamed itself our present name, Innovo Group Inc. Initially, we produced craft and accessory products for the consumer marketplace through various operating subsidiaries. Since that time, we gradually evolved from producing craft and accessory products to designing and selling apparel products. During this transition, we moved our operations from Tennessee to Los Angeles, California.

Our principal business activity has evolved into the design, development and worldwide marketing of apparel products, primarily, denim jeans and related casualwear. Our primary apparel products bear the brand name Joe s® operated under our Joe s Jeans Inc., or Joe s Jeans, subsidiary. Since Joe s Jeans was established in 2001, the brand is recognized in the premium denim industry for its quality, fit and fashion-forward designs. Because we focus on design, development and marketing, we rely on third party manufacturers to manufacture our apparel products for distribution and Pixior LLC, or Pixior, a Los Angeles-based distribution company, for product fulfillment services. We sell our products to numerous retailers, which include major department stores, specialty stores, and distributors around the world.

Fiscal 2006 was a transition year for us. After deciding to focus our operations on our Joe s® brand, we decided to cease operations of our other branded and private label business. In May 2006, we sold certain of the assets related to our private label division where we made denim apparel products for mass market retailers such as American Eagle Outfitters Inc., or AEO, and Target Corporation, or Target. In addition throughout the course of the fiscal year, we ceased production and sold the remaining indie and Betsey Johnson® inventory to focus on our Joe s® business. Further, in the third quarter of fiscal 2006, we began operating under an agreement with Pixior to outsource our product fulfillment services, including our warehousing, distribution and customer services needs for our products and moved our principal offices to space under a verbal facilities arrangement with Pixior.

To enhance our ability to capitalize on the Joe s® brand, on February 6, 2007, we entered into a merger agreement to merge with JD Holdings Inc., or JD Holdings, the successor in interest to JD Design LLC, or JD Design, the entity from whom we license the Joe s® brand. In exchange for all of the rights to the Joe s® brand and subject to approval by our stockholders, we will issue to JD Holdings 14,000,000 shares of our common stock, $300,000 in cash and enter into an employment agreement with Joe Dahan, the principal designer of the Joe s brand and sole stockholder of JD Holdings. In the event that the merger is approved, the license agreement will terminate and we will own all right, title and interest in the Joe s® brand and marks. By owning all rights to the Joe s® brand and marks outright, we will eliminate any risks associated with the potential termination of the license agreement and have the right to control the direction of the brand and our company, including licensing opportunities. To capitalize on licensing opportunities for the brand, we also announced that we entered into a license agreement with the Betesh Group to be effective upon completion of the merger agreement for the worldwide license to produce and sell handbags, belts and small leather goods, such as wallets for men and women bearing the Joe s® brand. We will receive a royalty of 10% on net sales of these products subject to certain minimums. The initial term of the license after it becomes effective will be through December 31, 2010 with certain renewal rights.

Principal Products and Revenue Sources

Our principal apparel products bear the Joe s® mark and operate under our Joe s Jeans subsidiary. Historically, our principal products also included private label denim and denim-related apparel products and other branded denim and denim-related apparel products bearing the indie , Betsey Johnson®, Fetish and Shago® marks operated under our Innovo Azteca Apparel, Inc., or IAA, subsidiary. Since the sale in May 2006 of certain assets of our private label business and subsequent classification as a discontinued operation, our continuing operations for fiscal 2006 only include net sales of our Joe s® brand and net sales of other terminated branded apparel lines. Because these other branded apparel lines were not separate operating divisions, the terminated lines are not included as part of our discontinued operations. They continue to be reflected in our overall net sales even though the brands will not be part of our continuing operations for fiscal 2007. We also sold the assets of our craft and accessory business operated under our Innovo subsidiary in May 2005 and reported that subsidiary as a discontinued operation as of fiscal 2004. For the previous three fiscal years, our net sales from continuing operations are as follows:

	(in thousands) **2006**	**2005**	**2004**
Joe s Jeans	$ 45,264	$ 33,304	$ 18,296
Other Branded	1,369	2,616	8,420
Total	$ 46,633	$ 35,920	$ 26,716

Joe s®

Through fiscal 2006 from fiscal 2004, our Joe s® brand represented approximately 97%, 93% and 68%, respectively, of our total net sales from continuing operations. This increase in percentage of overall net sales attributable to our Joe s® brand is indicative of our transition and decision to focus our resources on it and the reclassification of certain operations as discontinued.

Our Joe s® product line includes women s, men s and children s denim jeans, pants, shirts, sweaters, jackets and other apparel products sold domestically and internationally. Joe s® products are marketed to U.S. retailers through third party showrooms located in New York and Los Angeles and to international retailers through international distributors with showrooms in Paris, Tokyo and Germany. Joe s ® women s product line represents our largest source of revenue and consists primarily of denim jeans in a variety of different fits, fabrics, washes and detailing. Every season, we continue to offer certain core basic styles in addition to new ones to appeal to trendsetters and fashion forward consumers. We believe our attention to fitting different body styles gives us an advantage in the marketplace, as we can offer the consumer a product designed and tailored to fit her needs. We have branded the different fit styles so that the consumer can differentiate and choose from the variety carried by the retailer. Our fit styles currently include:

- Chelsea an ultra slim fit;
- Cigarette a straight and narrow fit;
- Honey a curvy fit;
- Lover a relaxed fit;
- Muse a higher waist fit;
- Provocateur a petite fit with a shorter inseam;
- Rocker a lean flare fit;
- Socialite a classic bootcut fit;

- Starlet a slim legged bootcut fit; and
- Twiggy a taller fit with a longer inseam.

Joe s® women s product offerings also include non-denim pants, denim skirts, denim and leather jackets, knit shirts, and sweaters. Suggested retail prices for Joe s® women s products currently range from $143 to $174 for denim and fashion pants, from $88 to $198 for tops and from $215 to $450 for jackets.

In the first quarter of fiscal 2006, Joe s® expanded its offerings by re-launching its men s denim line. Joe s® men s product line consists of men s denim jeans, in addition to non-denim pants, knit shirts, sweaters, and denim and leather jackets. We have carried over the concept from our women s line of offering a variety of different fits, fabrics, washes and detailing in our product selection. Similar to women s, we also offer for men certain core basic styles every season in addition to new styles. We also brand the fit styles, which include the Brixton, the Classic, the Rebel and the Rocker. Suggested retail prices for Joe s® men s products range currently from $158 to $289 for denim and fashion pants, from $62 to $168 for tops and from $158 to $795 for jackets.

Children s product offerings bearing the Joe s® brand first began selling in the first quarter of fiscal 2006 and include boy s, girl s and toddler s denim jeans and a limited selection of non-denim pants, tops and jackets. We do not participate in nor are we responsible for the product designs, manufacturing or sales of the children s products because we amended our master license agreement to release back these rights to JD Design. In exchange for this release, we receive royalty income of 5% on the net sales of the children s products. The royalty income received is included in our net sales.

Other Branded Apparel

Beginning in fiscal 2004, we terminated several of our branded apparel license agreements. In fiscal 2004, we terminated our license agreements for Fetish , Shago® and Hot Wheels® branded apparel. In July 2005, we terminated the license agreement associated with the Betsey Johnson® brand and in January 2006, we decided to exit the operation of our indie branded apparel line. During fiscal 2006, we had limited sales of other branded apparel bearing the indie and Betsey Johnson® marks. These sales related primarily to the liquidation of remaining inventory.

Private Label Apparel

From fiscal 2003 until May 2006, we also designed and developed private label apparel products under purchase order arrangements for mass market retailers. Our private label product line consisted of denim jeans for both the men s and women s market. Through private label arrangements, we sold denim products primarily to AEO and Target. In May 2006, we sold the assets of this division to Cygne Designs Inc., or Cygne, and now report this division as a discontinued operation. See Notes to Consolidated Financial Statements - Note 3 - Discontinued Operations for further discussion of the sale of these assets.

Product Design, Development and Sourcing

Joe s®

Our product development for the Joe s® brand is managed internally by a team of designers led by Joe Dahan, the owner of JD Design and president of our Joe s Jeans subsidiary. This design team is responsible for the creation, development and coordination of the product group offerings within each collection. Joe s® typically develops four collections per year for spring, summer, fall and holiday, with certain core basic styles offered throughout the year. Joe Dahan is an instrumental part of Joe s® design process. When we originally licensed the Joe s® brand from JD Design, we also entered into an employment agreement with Joe Dahan. The loss of Joe Dahan could have a material adverse impact on us; however, we believe we could find alternative sources for the development and design of Joe s products. The termination of employment of Joe Dahan would not affect our license agreement for the Joe s® brand. Furthermore, in connection with the proposed merger agreement, we have agreed to enter into a ten year employment contract with Joe Dahan for his services as the Creative Director of the brand to be effective as of the closing of the merger. While his current and proposed employment agreement both contain customary provisions related to continued employment, we believe that should Mr. Dahan s employment terminate, we would be able to find alternative sources for the development and design of Joe s® products. See Risk Factors The loss of the services of key personnel could have a material adverse effect on our business.

We currently rely on third party manufacturers to manufacture all of our products for distribution. Our manufacturers are primarily located in Mexico and the United States. For production in Mexico, we utilize an existing manufacturing relationship with a related party for the manufacture of our products. We purchase these products in various stages of production from partial to completed finished goods. We control the production schedules in order to ensure quality and timely deliveries. We outsource the warehousing, picking, packing and shipping of our Joe s® products to retailers to Pixior under an outsourcing agreement. We also share facilities with Pixior under a verbal lease arrangement. We purchase fabric for Joe s products both domestically and internationally from independent vendors. Our raw materials are principally blends of fabrics, yarns and threads and are available from multiple sources. We have not experienced any material shortage of raw material for our needs.

We continue to explore alternate inventory strategies designed to improve our gross margins. However, there can be no assurance that any change in sourcing will result in enhanced profit margins, similar quality or timely deliveries, but we do believe that continuing to monitor this expense can be beneficial for growth of our Joe s brand.

Other Branded Apparel

For other branded apparel lines that we no longer produce, we developed those products internally or in conjunction with design personnel of the licensor. Our Betsey Johnson® products were sourced from domestic contractors generally located in the Los Angeles area and our indie products were sourced from Mexico generally through Azteca Production International, Inc., or Azteca. Since we had not yet begun operating under our arrangement with Pixior, we were responsible for warehousing, packing and shipping our products to a warehouse which we previously shared under a verbal arrangement with Azteca and its affiliates for distribution directly to the retailer. We purchased fabric for these apparel lines both domestically and internationally from independent vendors.

General Product Sourcing

Historically, we relied on two of our stockholders, Hubert Guez and Paul Guez and their affiliated companies, including, Azteca and Commerce Investment Group LLC, or Commerce, for their experience and ability to source and supply our products. Initially, to assist with our transition from a craft and accessory business to the denim apparel and design business, we developed a strategic relationship with Hubert Guez and Paul Guez, Azteca and Commerce. Beginning in the summer of 2000, we entered into a series of transactions with them, including the issuance of securities, the execution of supply, manufacturing, warehousing and distribution agreements, and the acquisition of certain of their existing business units. The Guez brothers and their affiliated companies have in the aggregate more than fifty years of experience in the apparel industry with a specialty in denim apparel and related products.

While we have begun to reduce our reliance on our strategic relationship with the Guez s through the transitions of fiscal 2006, we currently utilize an Azteca subsidiary located in Mexico, AZT International SA de CV, or AZT, and its ability to manufacture our products on a purchase order basis. We purchase our products from them in various stages of production from partial to completed finished goods. We do not have a long-term supply agreement with them or any third party contractors, but we believe that there are a number of overseas and domestic contractors that could fulfill our requirements in the event that AZT would not be able to do so. Under our purchase order supply arrangement with AZT, during fiscal 2006, we purchased from AZT and its affiliates, approximately $12,845,000 or 55% of our products compared to $2,560,000, or 8%, in fiscal 2005, excluding products for our private label apparel division that we sold in May 2006 and report as a discontinued operation.

In the event we terminate our relationship with AZT in Mexico or the economic climate or other factors result in a significant reduction in the number of local contractors in the Los Angeles area, our business could be negatively impacted. At this time, we believe that we would be able to find alternative sources for the production of our apparel products if this were to occur; however, no assurances can be given that a transition could be completed without a short or long term disruption to our business.

We generally purchase our products in U.S. dollars. However, because we use some overseas or non-U.S. suppliers, the cost of these products may be affected by changes in the value of the relevant currencies. Certain of our apparel purchases in the international markets will be subject to the risks associated with the importation of these type products. See Business-Import Restrictions and Other Governmental Regulations.

While we attempt to mitigate our exposure to manufacturing risk, the use of independent contractors does reduce our control over production and delivery and exposes us to the usual risks of sourcing products from independent suppliers. Transactions with our foreign manufacturers and suppliers are subject to the typical risks of doing business abroad, generally, such as the cost of transportation and the imposition of import duties and restrictions. The United States and the countries in which our products are manufactured may, from time to time, impose new quotas, duties, tariffs or other restrictions, or adjust presently prevailing quotas, duty or tariff levels, which could affect our operations and our ability to import products at current or increased levels. We cannot predict the likelihood or frequency of any such events occurring. See Business - Import Restrictions and Other Governmental Regulations.

License Agreements and Trademarks

Joe s® License Agreement

In February 2001, we acquired license rights to the JD stylized logo and the Joe s® mark for most apparel and accessory products from JD Design. The license agreement has a ten-year term with two ten-year renewal periods subject to us not being in material default at the end of each period. Additionally, pursuant to the terms of the agreement, Joe Dahan receives a 3% royalty on the net sales of Joe s® products. We believe that we will be able to renew our Joe s® license; however, there can be no assurance that other factors may arise that could result in the non-renewal of this license.

On February 6, 2007, we entered into a merger agreement with JD Holdings, the successor-in-interest to JD Design, to acquire all right, title and interest in the Joe s® brand and related marks. In exchange for the rights to the Joe s® brand and subject to approval by our stockholders, we will issue to JD Holdings 14,000,000 shares of our common stock, $300,000 in cash and enter into an employment agreement with Joe Dahan, the principal designer of the Joe s brand and sole stockholder of JD Holdings. In the event that the merger is approved, the license agreement will terminate and we will own all right, title and interest in the Joe s® brand and the marks. By owning all rights to the Joe s® brand and marks outright, we will eliminate any risks associated with the potential termination of the license agreement and have the right to control the direction of the brand and our company. In addition, we also entered into a license agreement to be effective after completion of the merger agreement for the worldwide license for bags, belts and small leather goods, such as wallets for a royalty on the net sales. We expect that in the event the merger is approved and completed, we will seek additional license partners for the Joe s® brand.

As the licensee and on behalf of JD Design, we have applied for protection with the United States Patent and Trademark Office, as well as with various foreign jurisdictions, such as Australia, Canada, China, the European Union, Japan, Korea, India, New Zealand, Russian Federation, Singapore, Switzerland and Turkey for trademark protection for certain of Joe s logos and Joe s Jeans marks for apparel and accessory products. As of November 25, 2006, three trademark registrations for various stylized designs bearing variations of Joe s, Joe s Jeans and JD name and or logo have been issued, one has been allowed and one trademark registration for the Lover has been issued in the United States. Internationally, primarily under the Madrid Protocol, 38 trademark registrations have been issued and we continue to prosecute 22 pending trademark applications internationally that we believe are necessary to protect the brand.

Terminated Branded Apparel Lines

As we evaluated our business operations during fiscal 2004 through fiscal 2006, we terminated the operation of several of our branded apparel lines. A discussion of these branded apparel license agreements and rights is included to provide the reader with background information about these terminated branded apparel lines.

indie

In June 2004, we announced the launch and initial development of a new line of company-owned and designed branded denim and denim-related apparel bearing the brand name indie . The indie line was a collection of women s five-pocket denim jeans and skirts, tops and jackets utilizing our in-house denim design, production and marketing personnel. indie products began shipping in January 2005 and as a result of lower than anticipated sales and to further our strategy and focus on our Joe s® brand, in January 2006, we announced that we were exiting the operation of the indie brand. Over the course of fiscal 2006, we sold the remaining inventory. However, we continue to own the trademark applications that have been issued internationally.

Betsey Johnson® License Agreement

On July 22, 2005, we entered into a termination settlement agreement and mutual release with B.J. Vines, licensor of the Betsey Johnson® apparel brand, to provide for the immediate termination of the license agreement under which IAA had the exclusive right to design, market, and distribute women s denim and coordinating denim related apparel under the Betsey Johnson® brand name in the United States and Canada. Because of lower than anticipated sales, the parties believed that the termination of the agreement was in the best interest of the parties.

In exchange for the early termination of the license agreement and a general release by both parties, IAA paid to B.J. Vines a one-time payment in the amount of $350,000. This one time payment represented a significant amount less than the minimum guaranteed royalties that IAA would have otherwise been required to pay during the remaining three years of the license. In connection with the termination, IAA has no further obligations under the license agreement, and all ancillary documents, which included a personal guarantee by the original licensee, were also terminated. During fiscal 2006, we sold the limited amount of remaining inventory and beginning in the fourth quarter of fiscal 2006, we did not have any additional sales related to this terminated apparel line.

Fetish , Shago® and Hot Wheels®

During fiscal 2004, we terminated three other branded apparel licenses as a result of our decision to exit the urban apparel market and shift our focus and resources on denim and denim-related apparel. However, throughout the course of fiscal 2005, we continued to have some limited sales of excess inventory pursuant to our settlement agreements. As a result, these limited net sales of Fetish and Shago® branded apparel are included in net sales of other branded apparel for fiscal 2005. There were never any sales of the Hot Wheels® branded apparel line. We have no further obligations under our settlement agreements other than customary continuing rights related to indemnification, audits and maintenance of books and records.

Sales, Distribution and Outsourcing Agreements

Joe s®

Domestically, our Joe s® branded apparel products are sold to retailers and specialty stores through independent third party showrooms located in Los Angeles and New York where retailers review the latest collections offered by Joe s and place orders. The showroom representatives provide us with purchase orders from the retailers and other specialty store buyers. Pursuant to our arrangement with each of these showrooms, we pay sales commissions at an agreed upon percentage of sales less discounts, returns and other credit allowances. In addition, pursuant to our license agreement, we pay to JD Design a royalty of 3% on net sales. If the merger agreement is approved, we will no longer pay the royalty, but we will be obligated to pay certain additional salary amounts to Joe Dahan based upon gross profit and net sales. Under our outsourcing arrangement, Pixior warehouses, picks, packs and ships our Joe s products directly to the retailer or specialty store from its warehouse.

Internationally, we have sold our Joe s® branded apparel products through a Master Distribution Agreement, or MDA, with Beyond Blue Inc., or BBI, a Los Angeles-based company that specializes in international consulting, distribution and licensing for apparel products. Pursuant to the MDA entered into on January 1, 2004, Joe s granted to BBI the exclusive distribution rights for Joe s products outside the United States. Under the MDA s terms, BBI established sub-distributors and sales agents in certain international markets through sub-distribution arrangements and assumed our obligations under a prior agreement with Itochu Corporation, or Itochu, for the Japanese market. The initial term of the MDA was through June 30, 2007, with an option to renew under an amendment. Under the terms of the MDA, we sold our Joe s products to BBI at 22.5% discount from our wholesale price, which they then re-sold to various international retailers and sub-distributors. On February 1, 2007, we and BBI mutually agreed to dissolve the MDA. Under the terms of the dissolution, we have been assigned the rights associated with the sub-distributors in various countries and are continuing to work with existing international distributors in each country.

For the Japanese market, on July 1, 2003, Joe s entered into a three year Distribution and Licensing Agreement with Itochu pursuant to which Itochu obtained certain manufacturing and licensing rights for the Joe s® marks in Japan. As part of the MDA with BBI, we assigned our rights under the agreement with Itochu to BBI. The agreement with Itochu automatically ended on December 31, 2006, and we are currently working with them on a purchase order basis.

As a result of the dissolution of these two agreements, we are internally evaluating our options with respect to our international business and are reviewing our relationships in the international marketplace to create a strategy to improve and grow our international sales.

In April 2006, we announced that we entered into an agreement with Pixior to outsource our product fulfillment services, including our warehousing, distribution and customer services needs for our branded apparel products. We began operating under this agreement in the third quarter of fiscal 2006. In addition, in mid-July 2006, we moved our principal executive offices to space located within Pixior s current space under a verbal month to month arrangement for the use of general administrative offices. We pay Pixior $10,000 a month as a facility rent expense in addition to the fee we pay for our product fulfillment services.

Other Branded Apparel

For our other branded apparel lines, such as indie and Betsey Johnson®, we utilized a combination of internal sales, independent sales representative or third party showroom arrangements to meet with retailers to review the latest collections offered under the respective brand and place orders. In February 2005, we entered into a Master Distribution Agreement similar to our Joe s MDA with BBI for the international distribution of our indie products, which we mutually agreed to no longer operate under after our decision to exit the indie branded apparel line.

Advertising, Marketing and Promotion

Historically, our advertising campaign for our Joe s® brand has been limited to strategic placement of advertising in areas of high concentration of fashion advertising. We marketed through billboard advertisement in Los Angeles, California, and leased advertising space on the tops of taxi cabs in New York City. These advertising spaces have been outfitted with Joe s unique and eye-catching ads which primarily feature women s silhouettes. In addition, we have an internal public relations person to strategically place our products in magazines, editorials, and with stylists.

Sales through existing retail channels are enhanced by visual merchandising. For example, many of our customer s stores have denim focus areas located within a department that are dedicated to selling and showcasing our Joe s® merchandise on a year round basis.

Customers

Joe s®