JOE'S JEANS INC.
Form 10-Q
October 15, 2012
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended August 31, 2012

OR

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

For the transition period from to

Commission File Number: 0-18926

JOE S JEANS INC.

(Exact name of registrant as specified in its charter)

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

(323) 837-3700

(Registrant s telephone number, including area code)

NO CHANGE

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

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

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

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

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

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

The number of shares of the registrant s common stock outstanding as of October 15, 2012 was 66,965,373.

Table of Contents

JOE S JEANS INC.

QUARTERLY REPORT ON FORM 10-Q

Table of Contents

PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

	August 31, 2012 (unaudited)	November 30, 2011
ASSETS		
Current assets		
Cash and cash equivalents	$ 12,778	$ 12,690
Accounts receivable, net	1,436	1,542
Inventories, net	31,892	23,262
Due from related parties		612
Deferred income taxes, net	2,644	2,644
Prepaid expenses and other current assets	594	769
Total current assets	49,344	41,519
Property and equipment, net	5,901	5,464
Goodwill	3,836	3,836
Intangible assets	24,000	24,000
Deferred income taxes, net	4,663	4,663
Other assets	1,654	680
Total assets	$ 89,398	$ 80,162
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
Accounts payable and accrued expenses	$ 15,569	$ 10,499
Due to factor	2,712	3,265
Due to related parties	95	357
Total current liabilities	18,376	14,121
Deferred rent	1,658	1,284
Total liabilities	20,034	15,405
Commitments and contingencies		
Stockholders equity		
Common stock, $0.10 par value: 100,000 shares authorized, 67,183 shares issued and 66,854 outstanding (2012) and 65,477 shares issued and 65,148 outstanding (2011)	6,721	6,550
Additional paid-in capital	106,346	105,512
Accumulated deficit	(40,612)	(44,214)
Treasury stock, 329 shares	(3,091)	(3,091)
Total stockholders equity	69,364	64,757

Total liabilities and stockholders equity	$	89,398	$	80,162

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

1

Table of Contents

JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Three months ended		Nine months ended	
	August 31, 2012	August 31, 2011	August 31, 2012	August 31, 2011
	(unaudited)		(unaudited)	
Net sales	$ 30,304	$ 24,151	$ 84,906	$ 70,032
Cost of goods sold	16,486	14,407	44,444	38,382
Gross profit	13,818	9,744	40,462	31,650
Operating expenses				
Selling, general and administrative	10,778	10,919	31,935	30,053
Depreciation and amortization	363	323	979	887
Retail stores impairment		1,144		1,144
	11,141	12,386	32,914	32,084
Operating income (loss)	2,677	(2,642)	7,548	(434)
Interest expense	63	111	277	365
Income (loss) before provision for taxes	2,614	(2,753)	7,271	(799)
Income taxes (benefit)	1,224	(715)	3,669	298
Net income (loss)	$ 1,390	$ (2,038)	$ 3,602	$ (1,097)
Earnings (loss) per common share - basic	$ 0.02	$ (0.03)	$ 0.06	$ (0.02)
Earnings (loss) per common share - diluted	$ 0.02	$ (0.03)	$ 0.05	$ (0.02)
Weighted average shares outstanding				
Basic	65,676	64,128	65,319	63,871
Diluted	66,756	64,128	66,273	63,871

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

Table of Contents

JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Nine months ended August 31, 2012	Nine months ended August 31, 2011
	(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net cash provided by operating activities	$ 2,554	$ 7,986
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(1,520)	(1,825)
Net cash used in investing activities	(1,520)	(1,825)
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments to factor, net	(553)	(411)
Proceeds from exercise of options	20	
Payment of taxes on restricted stock units	(413)	(519)
Net cash used in financing activities	(946)	(930)
NET CHANGE IN CASH AND CASH EQUIVALENTS	88	5,231
CASH AND CASH EQUIVALENTS, at beginning of period	12,690	6,410
CASH AND CASH EQUIVALENTS, at end of period	$ 12,778	$ 11,641

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

Table of Contents

JOE S JEANS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(in thousands)

	Common Stock Shares	Common Stock Par Value	Additional Paid-In Capital	Accumulated Deficit	Treasury Stock	Total Stockholders Equity
Balance, November 30, 2010	64,131	$ 6,415	$ 104,364	$ (42,849)	$ (3,057)	$ 64,873
Net loss (unaudited)				(1,097)		(1,097)
Stock-based compensation, net of withholding taxes (unaudited)			821			821
Issuance of restricted stock (unaudited)	1,028	103	(103)			
Balance, August 31, 2011 (unaudited)	65,159	$ 6,518	$ 105,082	$ (43,946)	$ (3,057)	$ 64,597
Balance, November 30, 2011	65,477	$ 6,550	$ 105,512	$ (44,214)	$ (3,091)	$ 64,757
Net income (unaudited)				3,602		3,602
Exercise of stock options (unaudited)	20	2	18			20
Stock-based compensation, net of withholding taxes (unaudited)			985			985
Issuance of restricted stock (unaudited)	1,686	169	(169)			
Balance, August 31, 2012 (unaudited)	67,183	$ 6,721	$ 106,346	$ (40,612)	$ (3,091)	$ 69,364

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

Table of Contents

JOE S JEANS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The unaudited condensed consolidated financial statements of Joe s Jeans Inc., or Joe s, we or us, which include the accounts of our wholly-owned subsidiaries, for the three and nine months ended August 31, 2012 and 2011 and the related footnote information have been prepared on a basis consistent with our audited consolidated financial statements as of November 30, 2011 contained in our Annual Report on Form 10-K, or the Annual Report. Our fiscal year end is November 30.

Our principal business activity involves the design, development and worldwide marketing of apparel products. Our primary current operating subsidiary is Joe s Jeans Subsidiary Inc., or Joe s Jeans Subsidiary. Our primary assets include all rights, title and interest in the intellectual property, including the trademarks, related to the Joe s®, Joe s Jeans and JD® brand and marks, or the Joe s Brand. All significant inter-company transactions have been eliminated. We operate in two primary business segments: Wholesale and Retail. Our Wholesale segment is comprised of sales to retailers, specialty stores and distributors and includes expenses from marketing, sales, distribution and customer service departments. Also, some international sales are made directly to wholesale customers who operate retail stores. Our Retail segment is comprised of sales directly to consumers through full-price retail stores, outlet stores and through the *www.joesjeans.com/shop* internet site. We opened our first full price retail store in October 2008 in Chicago, Illinois and currently operate six full price retail stores and 17 outlet stores in outlet centers around the country. Our Corporate and other is comprised of expenses from corporate operations, which include the executive, finance, legal, and human resources departments, as well as design, production and general advertising expense to support the Joe s® brand.

These unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the related notes thereto contained in our Annual Report. In the opinion of management, the accompanying unaudited financial statements contain all adjustments (consisting of normal recurring adjustments), which management considers necessary to present fairly our financial position, results of operations and cash flows for the interim periods presented. The results for the three and nine months ended August 31, 2012 and 2011 are not necessarily indicative of the results anticipated for the entire year ending November 30, 2012. The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results may differ from those estimates.

NOTE 2 ADOPTION OF ACCOUNTING PRINCIPLES

There were no Financial Accounting Standards Board, or FASB, issued standards that we adopted in the relevant periods.

NOTE 3 ACCOUNTS RECEIVABLE, INVENTORY ADVANCES AND DUE TO FACTOR

Our primary method to obtain the cash necessary for operating needs has been through the sale of accounts receivable pursuant to factoring agreements and advances under inventory security agreements with our factor, CIT Commercial Services, a unit of CIT Group Inc., or CIT.

Table of Contents

As a result of these agreements, amounts due to factor consist of the following (in thousands):

	August 31, 2012	November 30, 2011
Non-recourse receivables assigned to factor	$ 16,994	$ 14,892
Client recourse receivables	51	108
Total receivables assigned to factor	17,045	15,000
Allowance for customer credits	(1,599)	(2,498)
Net loan balance from factored accounts receivable	(13,013)	(10,857)
Net loan balance from inventory advances	(5,145)	(4,910)
Due to factor	$ (2,712)	$ (3,265)
Non-factored accounts receivable	$ 1,980	$ 2,220
Allowance for customer credits	(298)	(358)
Allowance for doubtful accounts	(246)	(320)
Accounts receivable, net of allowance	$ 1,436	$ 1,542

Of the total amount of receivables sold by us as of August 31, 2012 and November 30, 2011, we hold the risk of payment of $51,000 and $108,000, respectively, in the event of non-payment by the customers.

CIT Commercial Services

Our Joe s Jeans Subsidiary is party to an accounts receivable factoring agreement and an inventory security agreement with CIT. The accounts receivable agreement gives us the ability to obtain cash by selling to CIT certain of our accounts receivable and the inventory security agreement gives us the ability to obtain advances for up to 50 percent of the value of certain eligible inventory. The accounts receivables are sold for up to 85 percent of the face amount on either a recourse or non-recourse basis depending on the creditworthiness of the customer. CIT currently permits us to sell our accounts receivables at the maximum level of 85 percent and allows advances of up to $6,000,000 for eligible inventory. CIT has the ability, in its discretion at any time or from time to time, to adjust or revise any limits on the amount of loans or advances made to us pursuant to both of these agreements and to impose surcharges on our rates for certain of our customers. In addition, cross guarantees were executed by and among us and all of our parent and subsidiaries to guarantee each entity s obligations. In connection with the agreements with CIT, certain assets are pledged to CIT, including all of the inventory, merchandise and/or goods, including raw materials through finished goods and receivables. However, our trademarks are not encumbered.

In May 2010, the parties amended the accounts receivable agreement to provide for a change in the factoring fees, an extension of the agreement and additional termination rights. The accounts receivable agreement may be terminated by CIT upon 60 days written notice or immediately upon the occurrence of an event of default as defined in the agreement. The accounts receivable agreement may be terminated by us upon 60 days written notice prior to June 30, 2013, or earlier provided that the minimum factoring fees have been paid for the respective period, or if CIT fails to fund us for five consecutive days. In the event the agreement is not terminated, it automatically extends for an additional year. The inventory agreement may be terminated once all obligations are paid under both agreements or if an event of default occurs as defined in the agreement.

Beginning July 1, 2010, we paid to CIT a factoring rate of 0.55 percent for accounts which CIT bears the credit risk, subject to discretionary surcharges, up to $40,000,000 of invoices factored, 0.50 percent over $40,000,000 of invoices factored and 0.35 percent for accounts which we bear the credit risk. The interest rate associated with borrowings under the inventory lines and factoring facility is 0.25 percent plus the Chase prime rate. As of August 31, 2012, the Chase prime rate was 3.25 percent.

Table of Contents

In the event we need additional funds, we have also established a letter of credit facility with CIT to allow us to open letters of credit for a fee of 0.25 percent of the letter of credit face value with international and domestic suppliers, subject to availability. At August 31, 2012, we did not have any letters of credit outstanding.

NOTE 4   INVENTORIES

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

	August 31, 2012	November 30, 2011
Finished goods	$ 20,076	$ 13,512
Finished goods consigned to others	304	238
Work in progress	2,863	2,052
Raw materials	9,990	8,574
	33,233	24,376
Less allowance for obsolescence and slow moving items	(1,341)	(1,114)
	$ 31,892	$ 23,262

We did not record any charges to our inventory reserve allowance for the three and nine month period ended August 31, 2012. For the three and nine months ended August 31, 2011, we record charges to our inventory reserve allowance of $128,000. During the third quarter of fiscal 2011, we wrote down certain finished goods inventory by $1,620,000, representing the lower of cost or market adjustment.

NOTE 5   PROPERTY AND EQUIPMENT

Property and equipment consisted of the following (in thousands):

	Useful lives (years)	August 31, 2012	November 30, 2011
Computer and equipment	3-7	$ 1,760	$ 1,753
Furniture and fixtures	3-7	3,550	2,453
Leasehold improvements, primarily retail	5-10	4,171	4,001
		9,481	8,207
Less accumulated depreciation		(3,580)	(2,743)
Net property and equipment		$ 5,901	$ 5,464

Depreciation and amortization expense related to property and equipment is recorded in operating expenses. For the three months ended August 31, 2012 and 2011, depreciation and amortization was $363,000 and $323,000, respectively, and for the nine months ended August 31, 2012 and 2011, was $979,000 and $887,000, respectively.

We review for indicators of impairment present at our retail stores (all located in the U.S) whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. These indicators of impairment are specifically related to under-performance or operating losses relative to expected historical or projected future operating results. We perform a recoverability test and an impairment test on these stores. The key assumptions used in estimates of projected cash flows were sales, gross margins and payroll costs. These forecasts are based on historical trends and take into account recent developments, as well as our future plans and intentions. Based upon the results of the discounted cash flow analysis, which included the operating performance of certain of our stores, we

Table of Contents

recorded an impairment charge related to property and equipment at two of our full price retail stores of $1,144,000 for both the three and nine months ended August 31, 2011 because we do not believe we can recover the carrying value of the property and equipment. There has been no impairment in the three and nine months ended August 31, 2012.

NOTE 6   RELATED PARTY TRANSACTIONS

As of August 31, 2012 and November 30, 2011, our related party balance consisted of amounts due to and due from certain related parties, as further described below, as follows (in thousands):

	August 31, 2012		November 30, 2011	
Due from related parties				
Ever Blue LLC	$		$	529
Albert Dahan				83
Total due from related parties	$		$	612
Due to related parties				
Joe Dahan	$	95	$	343
Albert Dahan				14
Total due to related parties	$	95	$	357

Joe Dahan

Mr. Dahan is entitled to a certain percentage of our gross profit on our Joe s® brand in any applicable fiscal year until October 2017. See   Note 10 - Contingent Consideration Payments   for a further discussion on the contingent consideration.

For the three and nine months ended August 31, 2012 and 2011, expenses of $462,000 and $439,000 and $1,394,000 and $1,342,000, respectively, were recorded in the statement of operations related to the contingent consideration payments made to Mr. Dahan under this agreement.

Albert Dahan

In April 2009, we entered into a commission-based sales agreement with Albert Dahan, brother of Joe Dahan, for the sale of our products into the off-price channels of distribution. Under the agreement, Mr. Albert Dahan is entitled to a commission for purchase orders entered into by us where he acts as a sales person. The agreement may be terminated at any time for any reason or no reason with or without notice. For the three months ended August 31, 2012 and 2011, payments of $137,000, and $165,000, respectively, and for the nine months ended August 31, 2012 and 2011, payments of $396,000 and $546,000, respectively, were made to Mr. Albert Dahan under this arrangement.

Effective as of June 1, 2009, we entered into a license agreement for the license of the children s product line with Kids Jeans LLC, or Kids LLC, an entity in which Mr. Albert Dahan holds an interest and has voting control. Under the terms of the license, Kids LLC had an exclusive right to produce, distribute and sell children s products bearing the Joe s® brand on a worldwide basis, subject to certain limitations on the channels of distribution. In exchange for the license, Kids LLC paid us a royalty payment of 20 percent on the first $5,000,000 in net sales, or $1,000,000. In April 2011, we terminated the license agreement and in June 2011, we entered into a settlement agreement with Kids LLC. Pursuant to the terms of the settlement agreement, Kids LLC agreed to pay to us approximately $450,000 in exchange for Kids LLC s right to continue to sell children s apparel products until September 30, 2011 or December 31, 2011, depending on the product to be sold and customer to whom it would be sold. In exchange, the parties entered into mutual releases with respect to all claims related to the subject matter. In October 2011, we entered into a new agreement, or New Agreement, similar to the foregoing license agreement with Kids LLC, with Ever Blue LLC, or Ever Blue, an entity

Table of Contents

which Albert Dahan is the sole member, for the continued sale of children s products. In exchange for the license, Ever Blue pays to us a royalty on net sales with certain guaranteed minimum sales for each term. For the nine months ended August 31, 2012, we have recognized $80,000 in royalty income under the New Agreement. In connection with the New Agreement, we provided initial funding to Ever Blue for inventory purchases. As of August 31, 2012, no amount was outstanding under this arrangement.

NOTE 7 EARNINGS PER SHARE

Earnings per share are computed using weighted average common shares and dilutive common equivalent shares outstanding. Potentially dilutive securities consist of outstanding options, restricted stock and unvested RSUs. A reconciliation of the numerator and denominator of basic earnings per share and diluted earnings per share is as follows:

	Three months ended (in thousands, except per share data)		Nine months ended (in thousands, except per share data)	
	August 31, 2012	**August 31, 2011**	**August 31, 2012**	**August 31, 2011**
Basic earnings (loss) per share computation:				
Numerator:				
Net income (loss)	$ 1,390	$ (2,038)	$ 3,602	$ (1,097)
Denominator:				
Weighted average common shares outstanding	65,676			