

JOE'S JEANS INC.  
Form 10-Q  
July 10, 2015  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended May 31, 2015

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 0-18926

**JOE S JEANS INC.**

(Exact name of registrant as specified in its charter)

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**Delaware**

(State or other jurisdiction of incorporation or organization)

**11-2928178**

(I.R.S. Employer Identification No.)

**2340 South Eastern Avenue, Commerce, California**

(Address of principal executive offices)

**90040**

(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.  Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  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

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

The number of shares of the registrant's common stock outstanding as of July 10, 2015 was 69,968,208.

Table of Contents

**JOE'S JEANS INC.**

**QUARTERLY REPORT ON FORM 10-Q**

	<b>Page</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	1
<u>Item 1. Financial Statements</u>	1
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	27
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	44
<u>Item 4. Controls and Procedures</u>	45
<b><u>PART II. OTHER INFORMATION</u></b>	45
<u>Item 1. Legal Proceedings</u>	45
<u>Item 1A. Risk Factors</u>	45
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	45
<u>Item 3. Defaults upon Senior Securities</u>	45
<u>Item 4. Mine Safety Disclosure</u>	46
<u>Item 5. Other Information</u>	46
<u>Item 6. Exhibits</u>	47
<b><u>SIGNATURES</u></b>	48

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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)

	May 31, 2015 (unaudited)	November 30, 2014
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 828	\$ 1,054
Accounts receivable, net	1,408	2,588
Factored accounts receivable, net	20,129	30,421
Inventories, net	48,579	61,319
Deferred income taxes, net	1,509	6,065
Prepaid expenses and other current assets	2,081	1,672
Total current assets	74,534	103,119
Property and equipment, net	4,580	5,040
Goodwill	12,230	12,230
Intangible assets	79,606	80,773
Deferred financing costs	1,400	1,611
Other assets	1,102	1,176
Total assets	\$ 173,452	\$ 203,949
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities		
Accounts payable and accrued expenses	\$ 16,064	\$ 23,331
Buy-out payable	3,277	3,277
Line of credit	20,820	31,338
Short-term debt	59,123	59,003
Total current liabilities	99,284	116,949
Convertible notes	26,078	24,733
Deferred income taxes, net	27,690	17,765
Deferred rent	3,001	2,862
Other liabilities	643	643
Total liabilities	156,696	162,952
Commitments and contingencies		
Stockholders' equity		
Common stock, \$0.10 par value: 100,000 shares authorized, 70,668 shares issued and 69,834 outstanding (2015) and	7,069	6,984

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69,822 shares issued and 69,298 outstanding (2014)

Additional paid-in capital	111,745	111,010
Accumulated deficit	(98,623)	(73,679)
Treasury stock, 834 shares (2015), 524 shares (2014)	(3,435)	(3,318)
Total stockholders' equity	16,756	40,997
Total liabilities and stockholders' equity	\$ 173,452	\$ 203,949

See accompanying notes to condensed consolidated financial statements.

Table of Contents**JOE S JEANS INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF NET LOSS AND COMPREHENSIVE LOSS****(in thousands, except per share data)**

	Three months ended		Six months ended	
	May 31, 2015	May 31, 2014	May 31, 2015	May 31, 2014
	(unaudited)		(unaudited)	
Net sales	\$ 47,229	\$ 48,167	\$ 90,246	\$ 95,511
Cost of goods sold	27,835	25,594	52,753	51,453
Gross profit	19,394	22,573	37,493	44,058
<b>Operating expenses</b>				
Selling, general and administrative	17,781	18,125	38,102	37,077
Depreciation and amortization	996	1,160	2,008	2,387
	18,777	19,285	40,110	39,464
Operating income (loss)	617	3,288	(2,617)	4,594
Interest expense	3,944	3,355	7,828	6,676
Other expenses/ (income)		(4,818)		(2,268)
Income (loss) before provision for taxes	(3,327)	4,751	(10,445)	186
Income tax expense	22	2,412	14,499	25
Net income (loss) and comprehensive income (loss)	\$ (3,349)	\$ 2,339	\$ (24,944)	\$ 161
<b>Earnings (loss) per common share - basic</b>	\$ (0.05)	\$ 0.03	\$ (0.36)	\$ 0.00
<b>Earnings (loss) per common share - diluted</b>	\$ (0.05)	\$ 0.01	\$ (0.36)	\$ 0.00
<b>Weighted average shares outstanding</b>				
Basic	69,355	68,148	69,139	68,045
Diluted	69,355	87,096	69,139	87,212

See accompanying notes to condensed consolidated financial statements.

Table of Contents**JOE S JEANS INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

	May 31, 2015	Six months ended (unaudited)	May 31, 2014
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net cash (used in) provided by operating activities	\$	10,841	\$ (4,039)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchases of property and equipment		(381)	(290)
Purchase of Hudson Clothing, Inc., net of cash acquired			(418)
Net cash used in investing activities		(381)	(708)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
(Repayment of) proceeds from line of credit		(10,518)	6,068
Repayment of term loan			(15)
Payment of promissory tax note			(1,235)
Purchase of restricted stock		(117)	(227)
Payment of taxes on restricted stock units		(51)	(205)
Net cash provided by (used in) financing activities		(10,686)	4,386
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>		<b>(226)</b>	<b>(361)</b>
CASH AND CASH EQUIVALENTS, at beginning of period		1,054	785
<b>CASH AND CASH EQUIVALENTS, at end of period</b>	<b>\$</b>	<b>828</b>	<b>\$ 424</b>

See accompanying notes to condensed consolidated 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
<b>Balance, November 30, 2013</b>	68,878	\$ 6,890	\$ 107,933	\$ (45,963)	\$ (3,091)	\$ 65,769
Net income (loss) and comprehensive income (loss) (unaudited)				161		161
Embedded conversion feature net of taxes (unaudited)			2,058			2,058
Stock repurchase (unaudited)					(227)	(227)
Stock-based compensation, net of withholding taxes (unaudited)			382			382
Issuance of restricted stock (unaudited)	641	64	(64)			
<b>Balance, May 31, 2014 (unaudited)</b>	69,519	\$ 6,954	\$ 110,309	\$ (45,802)	\$ (3,318)	\$ 68,143
<b>Balance, November 30, 2014</b>	69,822	\$ 6,984	\$ 111,010	\$ (73,679)	\$ (3,318)	\$ 40,997
Net income (loss) and comprehensive income (loss) (unaudited)				(24,944)		(24,944)
Stock repurchase (unaudited)					(117)	(117)
Stock-based compensation, net of withholding taxes (unaudited)			820			820
Issuance of restricted stock (unaudited)	846	85	(85)			
<b>Balance, May 31, 2015 (unaudited)</b>	70,668	\$ 7,069	\$ 111,745	\$ (98,623)	\$ (3,435)	\$ 16,756

See accompanying notes to condensed consolidated financial statements.



Table of Contents

**JOE S JEANS INC. AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 - BASIS OF PRESENTATION**

Our principal business activity involves the design, development and worldwide marketing of apparel products, which include denim jeans, related casual wear and accessories that bear the brand Joe s® and Hudson®. Our primary current operating subsidiaries are Joe s Jeans Subsidiary, Inc., or Joe s Jeans Subsidiary and Hudson Clothing, LLC, or Hudson. In addition, we have other subsidiaries, including Joe s Jeans Retail Subsidiary, Inc., Innovo West Sales, Inc., Hudson Clothing Holdings, Inc. and HC Acquisition Holding, Inc. All significant inter-company transactions have been eliminated. We completed the acquisition of Hudson on September 30, 2013 and the information presented includes the results of operations of Hudson from the date of acquisition.

Our reportable business segments are Wholesale and Retail. We manage, evaluate and aggregate our operating segments for segment reporting purposes primarily on the basis of business activity and operation. Our Wholesale segment is comprised of sales of Joe s® and Hudson® products to retailers, specialty stores and international distributors, includes revenue from licensing agreements and records expenses from sales, trade shows, distribution, product samples and customer service departments. Our Retail segment is comprised of sales to consumers through full price retail stores, outlet stores and through our online retail sites at [www.joesjeans.com](http://www.joesjeans.com) and [www.hudsonjeans.com](http://www.hudsonjeans.com). We opened our first full price retail store in October 2008 in Chicago, Illinois and we currently operate 12 full price retail stores and 20 outlet stores in outlet centers, malls and street locations around the country for our Joe s® brand. Our Corporate and other is comprised of expenses from corporate operations, which include the executive, finance, legal, human resources, design and production departments and general advertising expenses associated with our brands.

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

*Going Concern*

Prior to the acquisition of Hudson in fiscal 2013, our primary sources of liquidity were: (i) cash from sales of products; (ii) sales from accounts receivable factoring facilities and advances against inventory; and (iii) utilizing existing cash balances. In fiscal 2013, we incurred substantial indebtedness to finance the acquisition of Hudson, including approximately \$32,445,000 in the aggregate principal amount of convertible notes, a \$60,000,000 term loan credit agreement, and a \$50,000,000 revolving credit agreement.

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On November 6, 2014, we received an initial notice of default and event of default and demand for payment of default interest under the term loan credit facility for violating certain financial and maintenance covenants. As of May 31, 2015, we were not in compliance with the covenants under the term loan credit agreement. Under the term loan credit agreement, an event of default occurred because the minimum EBITDA for the twelve fiscal months ending (i) September 30, 2014 of \$22,136,300, (ii) October 31, 2014 of \$22,991,900, and (iii) November 30, 2014 of \$23,417,800 have not been met. In addition, as of May 31, 2015, the (i) financial plan and forecast for 2015 had not been timely delivered; (ii) minimum fixed charge coverage ratios at our respective quarter end measurement dates of 1.09x, 1.15x and 1.20x had not been met; and (iii) the maximum leverage ratios at our respective quarter end measurement dates of 3.21x, 3.00x and 2.75x had not been met. As a result of the events of default under the term loan credit agreement, this also triggered a default and an event of default under the terms of the revolving credit agreement. Both lenders have reserved their respective rights to exercise any and all remedies available to them under their respective agreements and have demanded payment of interest under those agreements at the default rate of interest. In addition, as a result of the events of default under the term loan credit agreement and the revolving credit agreement, we also became in default of our subordinated convertible notes issued to the former equity owners of Hudson. Under the terms of the revolving credit and term loan credit agreements, we are prohibited from making any payments under the subordinated convertible notes, but we are accruing interest on the convertible notes at the default rate. We are also prohibited from making earn-out payments to our creative director, Mr. Dahan under his buy-out agreement. On February 10, 2015, we received second notices of default and events of default for failure to comply with certain financial and other covenants and a demand for continued payment of default interest under the term loan credit agreement and revolving credit agreement from both Garrison Loan Agency Service LLC, or Garrison, and CIT Commercial Services, Inc., a unit of CIT Group, or CIT.

Table of Contents

In connection with the terms of the revolving and term loan credit agreements, certain restrictions were placed on our ability to incur indebtedness; create liens; consolidate, merge, liquidate or dissolve; sell, lease or otherwise transfer any assets; substantially change the nature of the business; make investments or acquisitions; pay dividends; enter into transactions with affiliates; amend material documents, prepay indebtedness and make capital expenditures. In addition, all of our assets, including trademarks, secure our obligations under the revolving and term loan credit agreements.

Our failure to cure the defaults could result in an acceleration of the debt by either or both lenders, which would have a material adverse effect on our liquidity, financial condition and results of operations, and could cause us to become bankrupt or insolvent. Since all of our assets are subject to liquidation by the creditors, liquidation could result in no assets being left for the stockholders after the creditors receive their required payment. On June 26, 2015, we entered into forbearance agreements and amendments to the revolving and term loan credit agreements with Garrison and CIT. Under the terms of the forbearance, the lenders have agreed to forbear from exercising certain of their respective rights and remedies with respect to each existing default (generally defined as existing and certain future anticipated or possible events of default) for a period of time. See Note 14 Subsequent Events for a further discussion of the forbearance agreements.

While management is evaluating all options to cure the defaults, including refinancing, extending the indebtedness and exploring all other alternatives for other sources of capital for ongoing cash needs, including a sale of assets or the company or a recapitalization, there can be no assurance that we will be able to secure a resolution or refinance or extend the indebtedness and, accordingly, our liquidity and ability to operate could be adversely affected. We have engaged Carl Marks Advisory Group to assist us as we explore all strategic and financing alternatives to resolve the defaults and events of default, including the engagement of a chief restructuring advisor to assist us with our day-to-day operational needs. We are currently in discussions with our creditors under both the term loan credit agreement and revolving credit agreement regarding a resolution to the defaults, and our ability to continue as a going concern is dependent upon us resolving the outstanding indebtedness.

As of May 31, 2015, our cash balance was \$828,000, our term loan had a balance of \$59,123,000 and our cash availability with CIT was approximately \$11,500,000. This amount with CIT fluctuates on a daily basis based upon invoicing and collection related activity by CIT on our behalf. As of May 31, 2015, our revolving credit facility had an outstanding balance of \$20,820,000.

As a result of the aforementioned defaults and events of default, Moss Adams LLP, our independent auditor, has expressed substantial doubt about our ability to continue as a going concern in their audit report dated February 13, 2015. The accompanying consolidated financial statements for the year ended November 30, 2014 and three and six months ended May 31, 2015 were prepared under the assumption that we will continue to operate as a going concern, which contemplates the realization of assets and the liquidation of liabilities in the ordinary course of business. As discussed in the previous paragraphs, we face various uncertainties that raise substantial doubt about our ability to continue as a going concern. These financial statements do not include any adjustments that may result from the outcome of these uncertainties.

**NOTE 2 ADOPTION OF ACCOUNTING PRINCIPLES**

In May 2014, the Financial Accounting Standards Board, or FASB, issued a comprehensive new revenue recognition standard which will supersede previous existing revenue recognition guidance. The standard creates a five-step model for revenue recognition that requires companies to exercise judgment when considering contract terms and relevant facts and circumstances. The five-step model includes (1) identifying the contract, (2) identifying the separate performance obligations in the contract, (3) determining the transaction price, (4) allocating the transaction price to the separate performance obligations and (5) recognizing revenue when each performance obligation has been satisfied. The standard also requires expanded disclosures surrounding revenue recognition. The standard is effective for fiscal periods beginning after December 15, 2016 and allows for either full retrospective or modified retrospective adoption. We are currently evaluating the

impact of the adoption of this standard on our consolidated financial statements.

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

Table of Contents

In May 2015, FASB issued ASU 2015-08, *Business Combinations (Topic 805): Pushdown Accounting - Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115*, or ASU 2015-08. The amendments in ASU 2015-08 amend various SEC paragraphs included in the FASB's Accounting Standards Codification to reflect the issuance of Staff Accounting Bulletin No. 115, or SAB 115. SAB 115 rescinds portions of the interpretive guidance included in the SEC's Staff Accounting Bulletins series and brings existing guidance into conformity with ASU No. 2014-17, *Business Combinations (Topic 805): Pushdown Accounting*, which provides an acquired entity with an option to apply pushdown accounting in its separate financial statements upon occurrence of an event in which an acquirer obtains control of the acquired entity. We have adopted the amendments in ASU 2015-08, effective May 8, 2015, as the amendments in the update are effective upon issuance. The adoption did not have an impact on our Condensed Financial Statements.

In April 2015, the FASB issued Accounting Standards Update No. 2015-03, *Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, or ASU 2015-03. ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. For public entities, ASU 2015-03 is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Early adoption is permitted for financial statements that have not been previously issued. ASU 2015-03 is to be applied on a retrospective basis and represents a change in accounting principle. We believe the adoption of ASU 2015-03 will not have a material effect on our consolidated financial statements.

**NOTE 3 FACTORED ACCOUNTS AND RECEIVABLES**

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

	May 31, 2015		November 30, 2014	
Non-recourse receivables assigned to factor	\$	24,831	\$	30,811
Client recourse receivables		1,192		7,878
Total receivables assigned to factor		26,023		38,689
Allowance for customer credits		(5,894)		(8,268)
Due from factor	\$	20,129	\$	30,421
Non-factored accounts receivable	\$	3,507	\$	4,264
Allowance for customer credits		(465)		(929)
Allowance for doubtful accounts		(1,634)		(747)
Accounts receivable, net of allowance	\$	1,408	\$	2,588

Of the total amount of receivables sold by us as of May 31, 2015 and November 30, 2014, we hold the risk of payment of \$1,192,000 and \$7,878,000, respectively, in the event of non-payment by the customers.

*CIT Commercial Services Amended and Restated Factoring Agreement*

On September 30, 2013, we entered into an amended and restated factoring agreement, or the Amended and Restated Factoring Agreement, with CIT, which replaced all prior agreements relating to factoring and inventory security. The Amended and Restated Factoring Agreement provides

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

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

Table of Contents

As of May 31, 2015, our cash balance was \$828,000 and our borrowing base cash availability with CIT was approximately \$11,500,000. This amount with CIT fluctuates on a daily basis based upon invoicing and collection related activity by CIT for the receivables sold. See also Note 13 Debt for a further discussion of our debt arrangements with CIT and other lenders and Note 14 Subsequent Events for a discussion of a forbearance agreement with CIT.

**NOTE 4 INVENTORIES, NET**

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

	May 31, 2015		November 30, 2014
Finished goods	\$ 31,276	\$	40,064
Finished goods consigned to others	1,055		1,089
Work in progress	2,316		4,424
Raw materials	17,446		19,408
	52,093		64,985
Less allowance for obsolescence and slow moving items	(3,514)		(3,666)
	\$ 48,579	\$	61,319

**NOTE 5 LONG-LIVED AND INTANGIBLE ASSETS AND GOODWILL***Valuation of Long-lived and Intangible Assets and Goodwill*

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

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

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



Table of Contents

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

Business acquisitions are accounted for under the purchase method by assigning the purchase price to tangible and intangible assets acquired and liabilities assumed. Assets acquired and liabilities assumed are recorded at their fair values and the excess of the purchase price over the amounts assigned is recorded as goodwill. Purchased intangible assets with finite lives are amortized over their estimated useful lives. Goodwill and intangible assets with indefinite lives are not amortized but are tested at least annually for impairment or whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

In fiscal 2007, we acquired through merger JD Holdings, which included all of the goodwill and intangible assets goodwill related to the Joe s®, Joe s Jeans and JD® logo and marks. On September 30, 2013, we acquired Hudson, which included all of the goodwill and intangible assets related to the Hudson® logos and marks. We have assigned an indefinite life to the remaining intangible assets relating to the trademarks acquired, and therefore, no amortization expenses are expected to be recognized. However, we will test the assets for impairment annually in accordance with our critical accounting policies.

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

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

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

**NOTE 6 RELATED PARTY TRANSACTIONS**

*Joe Dahan*

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

On February 18, 2013, we entered into a new agreement with Mr. Dahan that fixed the overall amount to be paid by us for the remaining months of year six through year 10 in the original merger agreement at \$9,168,000 through weekly installment payments beginning on February 22, 2013 until November 27, 2015. In the first quarter of fiscal 2013, we recorded a charge of \$8,732,000 as contingent consideration buy-out expense in connection with this agreement. This amount represented the net present value of the total fixed amount that Mr. Dahan would receive. The entire amount was expensed during the first quarter of fiscal 2013 as the amount payable represented a present obligation due to Mr. Dahan. On September 30, 2013, in connection with entry into new credit facilities relating to the acquisition of Hudson, Mr. Dahan, CIT, Garrison and all of our loan parties entered into an earn out subordination agreement, which provides, among other things, that any payment, whether in cash, in kind, securities or any other property, in connection with the our obligations to Mr. Dahan is expressly junior and subordinated in right of payment to all amounts due and owing upon any indebtedness outstanding under the revolving credit facility and the term loan facility. We are permitted to make certain amounts of weekly installment payments of our obligations in the absence of an insolvency proceeding or any event of default under the revolving credit agreement or the term loan credit agreement. As a result of our default under the revolving credit agreement or the term loan credit agreement, we are currently prohibited from making any payments to Mr. Dahan.

See Note 10 Commitments and Contingencies - Contingent Consideration Payments, Buy Out Agreement and Earnout Subordination Agreement for a further discussion on these agreements with Mr. Dahan.

Table of Contents

*Ambre Dahan*

In January 2013, we entered in to a consulting arrangement with Ambre Dahan, the spouse of Mr. Dahan, for design director services that paid her \$175,000 per annum on a bi-weekly basis. For the three months ended May 31, 2015 and 2014, we paid Ms. Dahan \$0 and \$40,000, and for the six months ended May 31, 2015 and 2014, we paid Ms. Dahan \$0 and \$87,000, respectively, under this arrangement. This arrangement was terminated effective as of November 17, 2014.

*Albert Dahan*

In October 2011, we entered into an agreement with Ever Blue LLC, or Ever Blue, an entity for which Albert Dahan is the sole member, for the sale of children's products. Ever Blue has an exclusive right to produce, distribute and sell children's products bearing the Joe's® brand on a worldwide basis, subject to certain limitations on the channels of distribution. In exchange for the license, Ever Blue pays to us a royalty on net sales with certain guaranteed minimum sales for each term. In connection with this agreement, we provided initial funding to Ever Blue for inventory purchases, which such amount has been repaid in full. For the three months ended May 31, 2015 and 2014, we recognized \$32,000 and \$60,000, respectively, in royalty income under the license agreement. For the six months ended May 31, 2015 and 2014, we recognized \$45,000 and \$308,000, respectively, in royalty income under the license agreement.

*Peter Kim*

We have entered into several agreements, including a stock purchase agreement, a convertible note, a registration rights agreement, an employment agreement and a non-competition agreement with Peter Kim, Chief Executive Officer of our Hudson subsidiary, in connection with the acquisition of Hudson. See Note 12 Acquisition of Hudson and Note 13 Debt for a further discussion of those agreements.

*Employment Agreements with Officers and Directors*

We have entered into employment agreements with Marc Crossman, our former President and Chief Executive Officer, Joe Dahan, our Creative Director and Peter Kim, our Chief Executive Office of our Hudson subsidiary. Mr. Dahan is also a member of our Board of Directors.

*Marc Crossman*

On May 30, 2008, we entered into an employment agreement with Mr. Crossman to serve as our President and Chief Executive Officer. The employment agreement was effective as of December 1, 2007, the commencement of our 2008 fiscal year, had an initial term of two years and automatically renewed for additional two year periods on December 1, 2009, December 1, 2011 and December 1, 2013, respectively. The employment agreement continues to automatically renew for additional two year periods if neither we nor Mr. Crossman provides 180 days

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advanced notice of non-renewal prior to the end of the term or upon the occurrence of a change in control. Under the employment agreement, Mr. Crossman is entitled to an annual salary of \$429,300, an annual discretionary bonus targeted at 50 percent of his base salary based upon the achievement of financial and other performance criteria that the Compensation and Stock Option Committee of the Board of Directors, or Compensation Committee, may deem appropriate in its sole and absolute discretion, an annual grant of equity compensation pursuant to our stock incentive plans, life and disability insurance policies paid on his behalf and other discretionary benefits that the Compensation Committee may deem appropriate in its sole and absolute discretion. The employment agreement provides for severance payment of up to two years if terminated under certain circumstances.

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

Table of Contents

*Joe Dahan*

On October 25, 2007, we entered into an employment agreement for Mr. Dahan to serve as Creative Director for the Joe's brand. The initial term of employment was for five years, or until October 25, 2012, and then automatically renewed for successive one year periods unless terminated earlier in accordance with the agreement. Under the employment agreement, Mr. Dahan is entitled to an annual salary of \$300,000 and other discretionary benefits that the Compensation Committee may deem appropriate in its sole and absolute discretion. The employment agreement provides for severance payment of up to one year if terminated under certain circumstances.

*Peter Kim*

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

*Hamish Sandhu*

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

**NOTE 7 EARNINGS PER SHARE**

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

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Table of Contents

	Three months ended		Six months ended	
	(in thousands, except per share data)		(in thousands, except per share data)	
	May 31, 2015	May 31, 2014	May 31, 2015	May 31, 2014
<b>Basic earnings (loss) per share computation:</b>				
Numerator:				
Net earnings (loss) and comprehensive earnings (loss)	\$ (3,349)	\$ 2,339	\$ (24,944)	\$ 161
Denominator:				
Weighted average common shares outstanding	69,355	68,148	69,139	68,045
<b>Earnings (loss) per common share - basic</b>				
Net earnings (loss) and comprehensive earnings (loss)	\$ (0.05)	\$ 0.03	\$ (0.36)	\$ 0.00
<b>Diluted earnings (loss) per share computation:</b>				
Numerator:				
Net earnings (loss) and comprehensive earnings (loss)	\$ (3,349)	\$ 2,339	\$ (24,944)	\$ 161
Convertible notes interest expense, net of taxes		557		1,960
Other Income - Gain from change in fair value of conversion derivative, net of taxes		(2,371)		(1,965)
Numerator for dilutive earnings (loss) per share	\$ (3,349)	\$ 525	\$ (24,944)	\$ 156
Denominator:				
Weighted average common shares outstanding	69,355	68,148	69,139	68,045
Effect of dilutive securities:				
Convertible note shares		18,430		18,369
Restricted shares, RSU s and options		518		798
Dilutive potential common shares	69,355	87,096	69,139	87,212
<b>Earnings (loss) per common share - diluted</b>				
Net earnings (loss) and comprehensive earnings (loss)	\$ (0.05)	\$ 0.01	\$ (0.36)	\$ 0.00

For the three months ended May 31, 2015, and 2014, currently exercisable options, convertible notes, unvested restricted shares and unvested RSUs in the aggregate of 20,599,927 and 21,510,929, respectively, have been excluded from the calculation of the diluted loss per share as their effect would have been anti-dilutive.

For the six months ended May 31, 2015, and 2014, currently exercisable options, convertible notes, unvested restricted shares and unvested RSUs in the aggregate of 20,599,927 and 21,510,929, respectively, have been excluded from the calculation of the diluted loss per share as their effect would have been anti-dilutive.

*Shares Reserved for Future Issuance*

As of May 31, 2015, shares reserved for future issuance include: (i) 563,000 shares of common stock issuable upon the exercise of stock options granted under the incentive plans; (ii) 667,169 shares of common stock issuable upon the vesting of RSUs; (iii) an aggregate of 2,557,438 shares of common stock available for future issuance under the Amended and Restated 2004 Stock Incentive Plan; and (iv) 18,969,425 shares of common stock issuable pursuant to the convertible notes.

**NOTE 8 INCOME TAXES**

We utilize the liability method of accounting for income taxes in accordance with FASB Accounting Standards Codification, or ASC, 740. Under the liability method, deferred taxes are determined based on the temporary differences between the financial statements and tax bases of assets and liabilities using enacted tax rates. For interim periods, the income tax provision is calculated using an estimated annual effective tax rate based upon projected annual income, permanent items, discrete items and statutory rates in states in which we operate.

A valuation allowance is required when it is more likely than not that all or a portion of a deferred tax asset will not be realized. Quarterly, management reassesses the need for a valuation allowance. Realization of deferred income tax assets is dependent upon taxable income in prior carryback years, estimates of future taxable income, tax planning strategies and reversals of existing taxable temporary differences. In determining the need for a valuation allowance, we reviewed all available evidence pursuant to the requirements of FASB ASC 740. Pursuant to ASC 740, we excluded the deferred income tax liabilities associated with identified indefinite long lived intangible assets as a source of income. For the first quarter of fiscal 2015, based upon our assessment of all available evidence, we have concluded that it is more likely than not that the net deferred tax assets, as of November 30, 2014, with

Table of Contents

the exception of certain deferred taxes associated with separate filing states for Hudson, will not be realized. For the first quarter of fiscal 2015, the valuation allowance associated with deferred taxes as of November 30, 2014, increased by \$14,481,000. Based on our prior assessment for fiscal 2014, 2013, and 2012, we had determined that the deferred tax assets were more likely than not to be realized with the exception of a valuation allowance of \$640,000, \$342,000 and \$0, respectively, that was recorded against a state net operating loss deferred tax asset. We considered all available evidence, both positive and negative, in our assessment of the valuation allowance needed as of February 28, 2015. Due to a review of operating performance for the quarter and a change in business strategy, which included the disposal of certain assets that have a fair value in excess of tax basis, we increased our valuation allowance by \$14,481,000 as of February 28, 2015. In calculating the amount of deferred tax assets subject to a valuation allowance, we have excluded the deferred tax liabilities associated with our trademarks from that amount. These intangible assets have an indefinite life and therefore, we cannot expect that the associated deferred tax liabilities will reverse over the same periods as our other net deferred tax assets. For the second quarter of fiscal 2015, based on our reassessment of the realizability of deferred taxes, we have determined that due to the operating performance for the quarter, a valuation allowance continues to be necessary for the deferred tax assets as of November 30, 2014, with the exception of certain deferred taxes associated with separate filing states for Hudson,

We are subject to U.S. federal income tax as well as income tax in multiple state jurisdictions. To the extent allowed by law, the tax authorities may have the right to examine prior periods where net operating losses were generated and carried forward, and make adjustments up to the amount of the net operating loss carryforward amount. We are no longer subject to U.S. federal and state income tax examinations by tax authorities for years prior to 2011 and 2010, respectively. We are currently not undergoing any examinations.

We had net operating loss carryforwards of \$25,067,000 at the end of fiscal 2014 for federal tax purposes that will expire from fiscal 2019 through 2034. We also had \$19,874,000 of net operating loss carryforwards available for California, which begin to expire from fiscal 2015 through fiscal 2034.

Certain limitations may be placed on net operating loss carryforwards as a result of changes in control as defined in Section 382 of the Internal Revenue Code. In the event a change in control occurs, it will have the effect of limiting the annual usage of the carryforwards in future years. Additional changes in control in future periods could result in further limitations of our ability to offset taxable income. Management believes that certain changes in control have occurred which resulted in limitations on our net operating loss carryforwards.

**NOTE 9 STOCKHOLDERS EQUITY**

*Stock Incentive Plans*

On June 3, 2004, we adopted the 2004 Stock Incentive Plan, or the 2004 Incentive Plan, and in October 2011, we adopted an Amended and Restated 2004 Stock Incentive Plan, or the Restated Plan, to update it with respect to certain provisions and changes in the tax code since its original adoption. Under the Restated Plan, the number of shares authorized for issuance is 6,825,000 shares of common stock. After the adoption of the Restated Plan in October 2011, we no longer grant awards pursuant to the 2004 Incentive Plan; however, it remains in effect for awards outstanding as of the adoption of the Restated Plan. Under the Restated Plan, grants may be made to employees, officers, directors and consultants under a variety of awards based upon underlying equity, including, but not limited to, stock options, restricted common stock,



restricted stock units or performance shares. The Restated Plan limits the number of shares that can be awarded to any employee in one year to 1,250,000. The exercise price for incentive options may not be less than the fair market value of our common stock on the date of grant and the exercise period may not exceed ten years. Vesting periods, terms and types of awards are determined by the Board of Directors and/or our Compensation Committee. The Restated Plan includes a provision for the acceleration of vesting of all awards upon a change of control as well as a provision that allows forfeited or unexercised awards that have expired to be available again for future issuance. Since fiscal 2008, we have issued both restricted common stock and RSUs to our officers, directors and employees pursuant to our various plans. The RSUs represent the right to receive one share of common stock for each unit on the vesting date provided that the employee continues to be employed by us. On the vesting date of the RSUs, we expect to issue the shares of common stock to each participant upon vesting and expect to withhold an equivalent number of shares at fair market value on the vesting date to fulfill tax withholding obligations. Any RSUs withheld or forfeited will be shares available for issuance in accordance with the terms of the Restated Plan.

The shares of common stock issued upon exercise of a previously granted stock option or a grant of RSUs are considered new issuances from shares reserved for issuance in connection with the adoption of the various plans. We require that the option holder provide a written notice of exercise in accordance with the option agreement and plan to the stock plan administrator and full payment for the shares be made prior to issuance. All issuances are made under the terms and conditions set forth in the applicable plan. As of May 31, 2015, 2,557,438 shares remained available for issuance under the Restated Plan.

Table of Contents

For all stock compensation awards that contain graded vesting with time-based service conditions, we have elected to apply a straight-line recognition method to account for all of these awards. For existing grants that were not fully vested at November 30, 2014, there was a total of \$871,000 and \$587,000 of stock based compensation expense recognized during the six months ended May 31, 2015 and 2014, respectively.

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

Granted as of:	May 31, 2015		Exercise price
		Number of options	
2002	40,000	\$	1.00
2002	31,496	\$	1.27
2003	30,768	\$	1.30
2004	320,000	\$	1.58
2005	300,000	\$	5.91
2006	450,000	\$	1.02

	Number of restricted shares issued
2007	320,000
2008	473,455
2009	371,436
2010	131,828
2011	
2012	617,449
2013	
2014	219,678
2015	

Exercise prices for all options outstanding as of May 31, 2015 were as follows:

Exercise Price	Options Outstanding and Exercisable	
	Number of shares	Weighted-Average Remaining Contractual Life
\$ 0.38	13,333	9.6
\$ 1.02	100,000	0.8
\$ 5.91	450,000	0.0
	563,333	0.4

Table of Contents

The following table summarizes stock option activity by plan for the six months ended May 31, 2015 and 2014 (in actual amounts):

	<b>Total Number of Shares</b>	<b>2004 Incentive Plan</b>	<b>Amended and Restated 2004 Incentive Plan</b>
Outstanding at November 30, 2014	550,000	550,000	
Granted	40,000		40,000
Exercised			
Forfeited / Expired	(26,667)		(26,667)
Outstanding and exercisable at May 31, 2015	563,333	550,000	13,333
Outstanding at November 30, 2013	775,000	775,000	
Granted			
Exercised			
Forfeited / Expired			
Outstanding and exercisable at May 31, 2014	775,000	775,000	

Table of Contents

Stock option activity in the aggregate for the periods indicated are as follows (in actual amounts):

	Options	Weighted average exercise price	Weighted average remaining contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at November 30, 2014	550,000	\$ 5.03		
Granted	40,000	0.38		
Exercised				
Expired				
Forfeited	(26,667)	0.38		
Outstanding and exercisable at May 31, 2015	563,333	\$ 4.91	\$ 0.4	\$
Weighted average per option fair value of options granted during the year		N/A		

	Options	Weighted average exercise price	Weighted average remaining contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at November 30, 2013	775,000	\$ 4.03		
Granted				
Exercised				
Expired				
Forfeited				
Outstanding and exercisable at May 31, 2014	775,000	\$ 4.03	0.9	\$
Weighted average per option fair value of options granted during the year		N/A		

As of May 31, 2015, there was \$631,000 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the 2004 Incentive Plan and the Restated Plan. That unrecognized compensation cost is expected to be recognized over a weighted-average period of 1.5 years.

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### Table of Contents

A summary of the status of restricted common stock and RSUs as of November 30, 2014 and November 30, 2013, and changes during the six months ended May 31, 2015 and 2014, are presented below (in actual amounts):

	Restricted Shares	Restricted Stock Units	Total Shares	Weighted-Average Grant-Date Fair Value	
				Restricted Shares	Restricted Stock Units
Outstanding at November 30, 2014	792,303	1,033,851	1,826,154	\$ 1.08	\$ 1.00
Granted	600,000		600,000	0.37	
Issued	(992,303)	(246,372)	(1,238,675)	0.94	1.09
Cancelled		(119,485)	(119,485)		0.97
Forfeited		(825)	(825)		0.70
Outstanding at May 31, 2015	400,000	667,169	1,067,169	\$ 0.37	\$ 0.98
Outstanding at November 30, 2013	954,798	1,661,330	2,616,128	\$ 0.90	\$ 0.93
Granted	288,121	362,242	650,363	1.49	1.49
Issued	(450,616)	(352,394)	(803,010)	0.95	1.06
Cancelled		(187,888)	(187,888)		0.98
Forfeited		(10,715)	(10,715)		0.70
Outstanding at May 31, 2014	792,303	1,472,575	2,264,878	\$ 1.08	\$ 1.04

In the three months ended May 31, 2015, we did not grant any shares of RSUs, options or restricted stock. In the six months ended May 31, 2015, we did not grant any shares of RSUs and granted 40,000 options to purchase shares of our common stock and 600,000 shares of restricted stock. In the three months ended May 31, 2015, we (i) issued 150,000 shares of restricted stock and common stock to holders of RSUs, respectively, in connection with the granting of restricted stock or vesting of RSUs or restricted stock. We did not withhold, cancel or forfeit any RSUs or retire into treasury any shares of restricted stock. In the six months ended May 31, 2015, we (i) issued 1,238,675 shares of restricted stock and common stock to holders of RSUs, respectively, in connection with the granting of restricted stock or vesting of restricted stock or RSUs, (ii) withheld, canceled or forfeited 120,310 RSUs, and (iii) retired into treasury 309,842 shares of restricted stock.

In the three months ended May 31, 2014, we did not grant any shares of RSUs, options or restricted stock. In the six months ended May 31, 2014, we granted 362,242 shares of RSUs and 288,121 shares of restricted stock. In the three months ended May 31, 2014, we (i) issued 58,914 shares of restricted stock and common stock to holders of RSUs, respectively, in connection with the granting of restricted stock or vesting of restricted stock or RSUs, (ii) withheld, canceled or forfeited 13,837 RSUs. We did not retire into treasury any shares of restricted stock. In the six months ended May 31, 2014, we (i) issued 803,010 shares of restricted stock and common stock to holders of RSUs, respectively, in connection with the granting of restricted stock or vesting of restricted stock or RSUs, (ii) withheld, canceled or forfeited 198,603 RSUs, and (iii) retired into treasury 194,901 shares of restricted stock.

### **NOTE 10 COMMITMENTS AND CONTINGENCIES**

#### *Contingent Consideration Payments, Buy-Out Agreement and Earnout Subordination Agreement*

As part of the consideration paid in connection with the merger with JD Holdings in October of 2007 and without regard to continued employment, until February 12, 2013, Mr. Dahan was entitled to a certain percentage of the gross profit earned by us in any applicable fiscal

year until October 2017. On February 18, 2013, we entered into an agreement with Mr. Dahan that provided certainty of payments to him by removing the contingencies related to the contingent consideration payments to be made to Mr. Dahan as an earn out under the original merger agreement. This agreement fixed the overall amount to be paid by us for the remaining months of year six through year 10 in the original merger agreement. The payments are now made over an accelerated time period until November 2015 instead of October 2017. Under the agreement, beginning on February 22, 2013 until November 27, 2015, Mr. Dahan is entitled to receive the total aggregate fixed amount of \$9,168,000 through weekly installment payments. In the first quarter of fiscal 2013, we recorded a charge of \$8,732,000 as contingent consideration buy-out expense in connection with this agreement. This amount represented the net present value of the total fixed amount that Mr. Dahan would receive. The entire amount was expensed during the first quarter of fiscal 2013 as the amount payable represented a present obligation due to Mr. Dahan. Mr. Dahan is not required to perform any services or remain employed to receive the fixed amount. Mr. Dahan also agreed to an additional restrictive covenant relating to non-competition and non-solicitation until November 30, 2016 that added to the original restrictive covenant in the merger agreement. As a result of our default under the revolving credit agreement or the term loan credit agreement, we are currently prohibited from making any payments to Mr. Dahan.

Table of Contents

*Operating Leases*

We lease retail store locations and our corporate offices and warehouse under operating lease agreements expiring on various dates through 2024 or 3 to 10 years from the rent commencement date. Some of these leases require us to make periodic payments for property taxes, utilities and common area operating expenses. Certain retail store leases provide for rents based upon the minimum annual rental amount and a percentage of annual sales volume, generally ranging from 6 percent to 8 percent, when specific sales volumes are exceeded. Some leases include lease incentives, rent abatements and fixed rent escalations, which are amortized and recorded over the initial lease term on a straight-line basis.

As of May 31, 2015, the future minimum rental payments under non-cancelable operating leases with lease terms in excess of one year were as follows (in thousands):

Future Lease Obligations are as follows (in thousands):

2015 Remainder of the year	\$	3,949
2016		7,818
2017		7,799
2018		7,628
2019		5,689
Thereafter		11,139
	\$	44,022

*Convertible Notes, Promissory Tax Notes, Revolving Credit Facility and Term Loan Credit Facility*

See Note 13 Debt for a further discussion on the commitments related to the acquisition of Hudson which included the issuance of the convertible notes, the tax notes, the revolving credit facility and the term loan credit facility.

Table of Contents**NOTE 11 SEGMENT INFORMATION**

The following table contains summarized financial information concerning our reportable segments:

	Three months ended		( dollar values in thousands )		Six months ended	
	May 31, 2015	May 31, 2014	May 31, 2015	May 31, 2014	May 31, 2015	May 31, 2014
<b>Net sales:</b>						
Wholesale	\$ 39,984	\$ 40,401	\$ 75,445	\$ 80,016		
Retail	7,245	7,766	14,801	15,495		
	\$ 47,229	\$ 48,167	\$ 90,246	\$ 95,511		
<b>Gross profit:</b>						
Wholesale	\$ 14,307	\$ 17,218	\$ 27,582	\$ 33,978		
Retail	5,087	5,355	9,911	10,080		
	\$ 19,394	\$ 22,573	\$ 37,493	\$ 44,058		
<b>Operating (loss) income:</b>						
Wholesale	\$ 8,394	\$ 11,560	\$ 16,186	\$ 21,931		
Retail	99	103	(508)	(885)		
Corporate and other	(7,876)	(8,375)	(18,295)	(16,452)		
	\$ 617	\$ 3,288	\$ (2,617)	\$ 4,594		

	May 31, 2015	Six months ended	May 31, 2014
<b>Capital expenditures:</b>			
Wholesale	\$ 381	\$	118
Retail			
Corporate and other			172
	\$ 381	\$	290

	May 31, 2015	November 30, 2014
<b>Total assets:</b>		
Wholesale	\$ 69,482	\$ 98,420
Retail	10,435	12,040
Corporate and other	93,535	93,489
	\$ 173,452	\$ 203,949

**NOTE 12 - ACQUISITION OF HUDSON**

On July 15, 2013, we announced the execution of a stock purchase agreement with Hudson, Fireman Capital CPF Hudson Co-Invest LP, or Fireman, Peter Kim, Paul Cardenas, Tony Chu, and certain option holders of Hudson named therein, pursuant to which we agreed to acquire all of the outstanding equity interests in Hudson. On September 30, 2013, we completed the acquisition of Hudson and purchased all of the outstanding equity interests for an aggregate purchase price of approximately \$94,102,000, consisting of \$65,416,000 in cash, approximately \$27,451,000 in convertible notes, net of discount, and \$1,235,000 in aggregate principal amount of promissory notes bearing no interest, that



was paid on April 1, 2014, to certain former option holders of Hudson.

In addition, in connection with the acquisition, we, along with all of our subsidiaries entered into: (i) a revolving credit agreement with CIT as administrative agent, collateral agent, documentation agent and syndication agent, CIT Finance LLC, as sole lead arranger and sole bookrunner, and the lenders party thereto, and (ii) a term loan credit agreement with Garrison, as administrative agent, collateral agent, lead arranger, documentation agent and syndication agent, and the lenders party thereto. In addition, we entered into an amended and restated factoring agreement with CIT that amends and restates our existing factoring agreement. See Note 13 Debt for a description of our debt arrangements.

Table of Contents

The acquisition has been accounted for as a purchase under United States generally accepted accounting principles. Accordingly, we have, with the assistance from independent valuation specialists, allocated the purchase price to the assets and liabilities of Hudson in our financial statements as of the completion of the acquisition at their respective fair values as of September 30, 2013. During the measurement period of one year, we recognized additional liabilities of \$2,003,000 based upon the information obtained from facts and circumstances that existed as of the acquisition date. Goodwill was increased by the same amount to reflect these adjustments.

The assets acquired in this acquisition consisted of tangible and intangible assets acquired and liabilities assumed. The differences between the fair value of the consideration paid and the estimated fair value of the assets and liabilities has been recorded as goodwill. The significant factors that resulted in recognition of goodwill were: (a) the purchase price was based upon cash flow and return on capital projections assuming integrations with our company and (b) the calculation of the fair value of tangible and intangible assets acquired that qualified for recognition. We have determined that the useful life of the acquired trade name asset is indefinite, and therefore, no amortization expense will initially need to be recognized. The useful life of the acquired customer relationships and design assets are finite and will be amortized over their useful lives. However, we will test the assets for impairment annually and/or if events or changes in circumstances indicate that the assets might be impaired. Additionally, a deferred tax liability has been established in the allocation of the purchase price with respect to the identified indefinite long lived intangible assets acquired.

Table of Contents

Under the purchase method of accounting, the total consideration as shown in the table below (in thousands) is allocated to the assets based on their estimated fair values as of the date of the completion of the acquisition. The consideration is allocated as follows:

Assets and liabilities assumed:	
Cash and cash equivalents	\$ 198
Accounts receivable	1,263
Due from factor	13,806
Inventories	22,230
Prepaid expenses and other assets	2,183
Property and equipment	726
Other assets	239
Accounts payable and accrued expenses	(9,566)
Other current liabilities	(3,132)
Due to factor	(7,411)
Deferred income taxes, net	(17,913)
Intangible assets acquired:	
Trade names	44,400
Customer relationships	2,700
Design	12,400
Net assets acquired	62,123
Goodwill created by the acquisition	31,979
Total consideration transferred	\$ 94,102
Total Purchase Price	
Cash	\$ 65,416
Promissory notes	1,235
Convertible notes (Face value \$32,445 less discount)	27,451
Total Purchase Price	\$ 94,102

**NOTE 13 - DEBT**

The five-year payment schedule of our term debt and convertible notes is as follows (in thousands):

	Total	Payments due by period (in thousands)					Thereafter
		2015	2016	2017	2018	2019	
Short term debt	\$ 59,123	\$ 59,123	\$	\$	\$	\$	\$
Convertible notes	33,766					33,766	
	\$ 92,889	\$ 59,123	\$	\$	\$	\$ 33,766	\$

Table of Contents

*Convertible Notes*

The convertible notes were issued with different interest rates and conversion features for Hudson's management stockholders and Fireman, respectively. Interest on the convertible notes is paid in a combination of cash and additional paid in kind notes, or PIK notes. Convertible notes in an aggregate principal amount of approximately \$22,885,000 (face amount) were issued to Hudson's management stockholders, are structurally and contractually subordinated to our senior debt and mature on March 31, 2019. All of the notes are expressly junior and subordinated in right of payment to all amounts due and owing upon any indebtedness outstanding under the revolving credit facility and the term loan facility (as discussed below).

The management notes accrue interest quarterly on the outstanding principal amount (i) from September 30, 2013 until the earlier to occur of the date of conversion of the notes or November 30, 2014 at a rate of 10 percent per annum, which is payable 7.68 percent in cash and 2.32 percent in PIK Notes, (ii) from December 1, 2014 until the earlier to occur of the date of conversion of the notes or September 30, 2016 at a rate of 10 percent per annum payable in cash, and (iii) from October 1, 2016 until the earlier to occur of the date of conversion of the notes or the date such principal amount is paid in full at a rate of 10.928 percent per annum payable in cash. Payment of interest at the cash pay rate under clause (ii) or (iii), as applicable, for any payment date will be subject to satisfaction of certain financial conditions for us. As of December 1, 2014, we did not meet such financial conditions, and therefore, the interest continues to accrue quarterly at a rate of 10 percent per annum, which is payable 7.68 percent in cash and 2.32 percent in PIK notes. In addition, because we are prohibited from making any payments under the subordinated convertible notes, as of January 1, 2015, we began to accrue an additional two percent interest under the default rate in cash. The management notes become convertible by each of the holders beginning on September 30, 2015 until maturity on March 31, 2019 into shares of our common stock, cash, or a combination of cash and common stock, with the settlement choice at our election.

The approximately \$9,560,000 (face amount) in aggregate principal amount of convertible notes issued to Fireman are structurally and contractually subordinated to our senior debt and mature on March 31, 2019. The Fireman note accrues interest quarterly on the outstanding principal amount (i) from September 30, 2013 until the earlier to occur of the date of conversion of the notes or November 30, 2014 at a rate of 6.5 percent per annum, which is payable 3 percent in cash and 3.5 percent in PIK Notes, (ii) from December 1, 2014 until the earlier to occur of the date of conversion of the notes or September 30, 2016 at a rate of 6.5 percent per annum payable in cash, and (iii) from October 1, 2016 until the earlier to occur of the date of conversion of the notes or the date such principal amount is paid in full at a rate of 7 percent per annum payable in cash. Payment of interest at the cash pay rate under clause (ii) or (iii), as applicable, for any payment date will be subject to satisfaction of certain financial conditions for us. As of December 1, 2014, we did not meet such financial conditions, and therefore, the interest continues to accrue quarterly at a rate of 6.5 percent per annum, which is payable 3 percent in cash and 3.5 percent in PIK notes. In addition, because we are prohibited from making any payments under the subordinated convertible notes, as of January 1, 2015, we began to accrue an additional two and a half percent interest under the default rate in cash. The Fireman note becomes convertible by the holder on October 14, 2014 until maturity on March 31, 2019 into shares of common stock, cash, or a combination of cash and common stock, with the settlement choice at our election.

Each of the notes is convertible, in whole but not in part, at a conversion price of \$1.78 per share, subject to certain adjustments, into approximately 18,200,000 shares of our common stock. The Fireman note may be converted at its sole election and the management notes may be converted at either a majority of the holders' election or individually, depending on the holder. If we elect to pay cash with respect to a conversion of the notes, the amount of cash to be paid per share will be equal to (a) the number of shares of common stock issuable upon such conversion multiplied by (b) the average of the closing prices for the common stock over the 20 trading day period immediately preceding the notice of conversion. We will have the right to prepay all or any portion of the principal amount of the notes at any time by paying 103 percent of the principal amount of the portion of any management note subject to prepayment or 100 percent of the principal amount of the portion of the Fireman note subject to prepayment.

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The holders of the convertible notes also have demand and piggyback registration rights associated with their notes in a separate agreement pursuant to which they have the right to require us to prepare and file a registration statement on Form S-1 or S-3 or any similar form or successor to such forms under the Securities Act, or any other appropriate form under the Securities Act or the Exchange Act, for the resale of all or part of their shares that may be issued under the convertible notes.

### *Embedded Conversion Derivative*

FASB Accounting Standards Codification (ASC) Topic 470 (ASC 470), *Accounting for Convertible Debt Instruments That May be Settled in Cash upon Conversion (Including Partial Cash Settlement)* requires the issuer of convertible debt that may be settled in shares or cash upon conversion at their option, such as our convertible notes, to account for their liability and equity components separately by bifurcating the embedded conversion derivative, or the derivative, from the host debt instrument. Although ASC 470 has no impact on our actual past or future cash flows, it requires us to record non-cash interest expense as the debt discount is amortized.

Table of Contents

As a result of the issuance of convertible notes in September 2013, the total potential shares of common stock that could be issued exceeded the amount of shares we were eligible to issue under NASDAQ rules as of that date. Therefore, we were required to value the derivative and recognize the fair value as a long-term liability. The fair value of this derivative at the time of issuance of the convertible notes was \$5,496,000 and was recorded as the original debt discount for the purposes of accounting for the debt component of the convertible notes. This debt discount on the Fireman and management notes are being amortized as interest expense using an effective interest rate of 8.32 percent and 4.31 percent, respectively, over the remaining 5.5 year term of the convertible notes.

On May 8, 2014, we obtained stockholder approval for our ability to issue the common stock underlying the convertible notes in compliance with NASDAQ rules. The derivative liability has been reassessed and it was determined that it should be reclassified to stockholders' equity as of May 8, 2014. We determined the fair value of the derivative using a binomial lattice model at that date. The key assumptions for determining the fair value at May 8, 2014 included the remaining time to maturity of approximately four years and ten months, volatility of 60 percent, and the risk-free interest rate of 1.63 percent. The fair value of the embedded conversion derivative was \$5,700,000 and \$3,430,000 at November 30, 2013 and May 8, 2014, respectively. The decrease in the fair value of the embedded conversion derivative from November 30, 2013 to May 8, 2014 resulted in a gain of \$2,270,000, which has been recorded as other income. The primary reason for the decrease in fair value was due to the change in our stock price as compared to the conversion price.

The following table (in thousands) is a summary of the recorded value of the convertible note as of May 31, 2015. The value of the convertible note reflects the present value of the contractual cash flows from the convertible notes and resulted in an original issue discount of \$10,490,000 including the additional original discount attributed to the embedded conversion derivative of \$5,496,000, that were recorded on September 30, 2013, the issuance date.

	<b>Balance May 31, 2015</b>
Convertible notes - Face value	\$ 32,445
Less: Original issue discount	(4,994)
Less: Debt discount related to the embedded derivative liability	(5,496)
Convertible notes recorded value on issue date	21,955
Add: PIK notes issued	1,321
Accretion of debt discounts	2,802
Convertible notes value	26,078

The following table (in thousands) is a summary of our total interest expense as follows:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>May 31, 2015</b>	<b>May 31, 2014</b>	<b>May 31, 2015</b>	<b>May 31, 2014</b>
Contractual coupon interest	\$ 3,332	\$ 2,791	\$ 6,599	\$ 5,543
Amortization of discount and deferred financing costs	612	564	1,229	1,133
Total interest expense	\$ 3,944	\$ 3,355	\$ 7,828	\$ 6,676

*Promissory Notes*

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In connection with the acquisition of Hudson, we issued approximately \$1,235,000 in aggregate principal amount of promissory notes bearing no interest that were paid on April 1, 2014 to certain option holders of Hudson.

### *Revolving Credit Agreement*

The revolving credit agreement with CIT provides us with a revolving credit facility up to \$50,000,000 comprised of a revolving A-1 commitment of up to \$1,000,000 and a revolving A commitment of up to \$50,000,000 minus the revolving A-1 commitment. Our actual maximum credit availability under the revolving facility varies from time to time and is determined by calculating a borrowing base, which is based on the value of the eligible accounts receivable and eligible inventory minus reserves imposed by CIT. The revolving facility also provides for swingline loans, up to \$5,000,000 sublimit, and letters of credit, up to

Table of Contents

\$1,000,000 sublimit. Proceeds from advances under the revolving facility may be used for working capital needs and general corporate purposes and were initially used to pay a portion of the consideration for the acquisition of Hudson and fees and expenses associated with the acquisition of Hudson. As of May 31, 2015, \$20,820,000 was outstanding under our revolving credit facility and cash availability of approximately \$11,500,000.

All unpaid loans under the revolving facility mature on September 30, 2018. We have the right at any time and from time to time to terminate the commitments under the revolving facility by paying in full or prepay any borrowings, in whole or in part, without terminating or reducing the commitment. If we terminate the revolving facility in full prior to the second anniversary of the date, we are required to pay a prepayment fee of 1 percent or 0.5 percent of the commitments terminated depending on when we make the prepayment.

The revolving facility is guaranteed by us and all of our subsidiaries, and secured by liens on substantially all assets owned by us, including a first- priority lien on certain property, including principally trade accounts, inventory, certain related assets and proceeds of the foregoing, subject to permitted liens and exceptions, and a second-priority lien on all other assets, including intellectual property owned by us, which secures the term loan facility on a first-priority basis.

Advances under the revolving facility are in the form of either base rate loans or LIBOR rate loans. The interest rate for base rate loans under the revolving A commitment fluctuates and is equal to (x) the Alternate Base Rate, which is the greatest of (a) the JPMorgan Chase Bank prime rate; (b) the Federal funds rate plus 0.50 percent; and (c) the 90-Day LIBO Rate, which is the rate per annum equal to the 90 day LIBOR published in the New York City edition of the Wall Street Journal under Money Rates, plus 1 percent, in each case, plus (y) 1.5 percent. The interest rate for LIBOR rate loans under the revolving A commitment is equal to the 90-Day LIBO Rate per annum plus 2.5 percent. The interest rate for base rate loans and LIBOR rate loans under the revolving A-1 commitment is equal to (i) Alternate Base Rate plus 2.5 percent and (ii) the 90-Day LIBO Rate plus 3.5 percent, respectively. Interest on the revolving facility is payable on the first day of each calendar month and the maturity date. In addition, because we are in default under the revolving credit facility, we are paying an additional one percent interest under the default rate. Our average interest rate, including the default rate, is approximately 3.5 percent. Among other fees, we pay a commitment fee of 0.25 percent per annum (due quarterly) on the average daily amount of the unused revolving commitment under the revolving facility. We also pay fees with respect to any letters of credit.

The revolving facility contains usual and customary negative covenants for transactions of this type, including, but not limited to: restrictions on our ability and our subsidiaries' ability, to create or incur indebtedness; create liens; consolidate, merge, liquidate or dissolve; sell, lease or otherwise transfer any of its assets; substantially change the nature of its business; make investments or acquisitions; pay dividends; enter into transactions with affiliates; and amend material documents, prepay certain indebtedness and make capital expenditures. The negative covenants are subject to certain exceptions as specified in the revolving credit agreement.

In addition, the revolving credit agreement requires us to: (a) maintain (i) at all times availability under the revolving facility of not less than \$5,000,000 and (ii) at all times the sum of availability under the revolving facility plus up to \$2,500,000 of unrestricted cash of not less than \$7,500,000; and (b) maintain a minimum fixed charge coverage ratio calculated for each four fiscal quarter period at levels set forth in the revolving facility.

As of May 31, 2015, we were not in compliance with certain covenants under the revolving credit agreement as a result of an event of default under the term loan credit agreement. As of November 30, 2014, we were out of compliance with the minimum fixed charge coverage ratio of 1.09x and had failed to timely deliver the financial plan and forecast for 2015. As of February 28, 2015, the (i) fixed charge



coverage ratio of 1.15x and (ii) leverage ratio of 3.00x were also not met. As of May 31, 2015, the (i) fixed charge coverage ratio of 1.20x and (ii) leverage ratio of 2.75x were not met.

See Note 14- Subsequent Events for a discussion of forbearance agreements and amendments to the revolving credit and term loan credit agreements entered into with CIT and Garrison.

*Term Loan Credit Agreement*

The term loan credit agreement entered into with Garrison provided for term loans of up to \$60,000,000 and was fully funded to us as of September 30, 2013. The term loan proceeds were used to finance a portion of the consideration for the acquisition of Hudson, to pay fees and expenses associated with the acquisition and for working capital needs and other general corporate purposes.

Table of Contents

The term loan matures on September 30, 2018. We are allowed to prepay the term loan at any time, in whole or in part, subject to the payment of a prepayment fee if we prepay prior to September 30, 2016. The prepayment fee is 3 percent if we prepay prior to September 30, 2014 and reduces by 1 percent per year until September 30, 2016. In addition, we are required to make prepayments out of extraordinary receipts, certain percentage of the excess cash flow and certain net proceeds of certain asset sales or equity issuances, in each case (other than a prepayment in connection with excess cash flow), subject to the payment of the prepayment fee as set forth above.

The term loan facility is guaranteed by us and all of our subsidiaries and is secured by liens on substantially all assets owned by us, including a first-priority lien on intellectual property owned by us and a second-priority lien on the revolving credit priority collateral.

The interest rate for the term loan fluctuates and is equal to the rate per annum equal to the British Banker Association Interest Settlement Rate for deposits in Dollars with a term of three months, as appears on the Bloomberg BBAM Screen, plus 10.75 percent. Interest is payable on the first day of each calendar month and the maturity date. In addition, because we are in default under the term loan agreement, we are paying an additional two percent interest under the default rate. Our average interest rate, including the default rate, is approximately 14 percent.

The term loan credit agreement contains usual and customary negative covenants for transactions of this type, including, but not limited to, restrictions on our ability and our subsidiaries' ability to create or incur indebtedness; create liens; consolidate, merge, liquidate or dissolve; sell, lease or otherwise transfer any of its assets; substantially change the nature of its business; make investments or acquisitions; pay dividends; enter into transactions with affiliates; amend material documents, prepay certain indebtedness and make capital expenditures. The negative covenants are subject to certain exceptions as specified in the term loan credit agreement.

In addition, the term loan credit agreement also requires us to maintain: (a) (i) at all times, availability under the revolving credit facility of not less than \$5,000,000 and (ii) at all times as tested on each date that a borrowing certificate is delivered, the sum of availability under the revolving credit facility plus up to \$2,500,000 of unrestricted cash of not less than \$7,500,000; (b) a minimum fixed charge coverage ratio; (c) a minimum EBITDA; and (d) a leverage ratio not more than the maximum leverage coverage ratio as set forth in the term loan credit agreement.

As of May 31, 2015, we were not compliance with certain covenants under the term loan credit agreement. Under the term loan credit agreement, an event of default has occurred. The minimum EBITDA for the twelve fiscal months ending (i) September 30, 2014 of \$22,136,300, (ii) October 31, 2014 of \$22,991,900 and (iii) November 30, 2014 of \$23,417,800 were not met. In addition, as of November 30, 2014, we were out of compliance with the (i) minimum fixed charge coverage ratio of 1.09x; and (ii) the maximum leverage ratio of 3.21x. As of February 28, 2015, the (i) fixed charge coverage ratio of 1.15x; and (ii) leverage ratio of 3.00x were also not met. As of May 31, 2015, the (i) fixed charge coverage ratio of 1.20x; and (ii) leverage ratio of 2.75x were not met. As a result of being out of compliance with these covenants, the term loan debt has been classified as current on the balance sheet.

See Note 14- Subsequent Events for a discussion of forbearance agreements and amendments to the revolving credit and term loan credit agreements entered into with CIT and Garrison.

*Amended and Restated Factoring Agreement*

See Note 3 Factored Accounts and Receivables for a discussion of our Amended and Restated Factoring Agreement.

**NOTE 14 SUBSEQUENT EVENTS**

On June 26, 2015, we entered into a Forbearance and Amendment No. 3 to Revolving Credit Agreement, or the CIT Forbearance Agreement, with CIT. The CIT Forbearance Agreement requires CIT and the lenders to forbear from exercising certain of their respective rights and remedies with respect to each existing default (generally defined as existing and certain future anticipated or possible events of default) under the revolving credit agreement during the forbearance period and further amends the revolving credit agreement.

Concurrent with the CIT Forbearance Agreement, we entered into a substantially similar forbearance agreement with Garrison, or the Garrison Forbearance Agreement, that also amended the term loan credit agreement. The CIT Forbearance Agreement and Garrison Forbearance Agreement are collectively referred to as the Forbearance Agreements.

Both of the Forbearance Agreements provide that each of the lenders will forbear from exercising certain of their respective rights and remedies during the forbearance period with respect to existing defaults. The Forbearance Period ends upon the earliest to occur of a Forbearance Default or October 15, 2015, or the Forbearance Termination Date. The Forbearance Period is automatically extended until November 15, 2015 if at the Forbearance Termination Date no Forbearance Default has occurred and all of the milestones with respect to a sale/recapitalization process have been met, except for shareholder approval, or the Extended Forbearance

Table of Contents

Termination Date. To induce the lenders to enter into the Garrison Forbearance Agreement, we have agreed to pay a forbearance fee of 1.35% of the greater of the outstanding balance of the obligations under the term loan credit agreement on (i) June 26, 2015 or (ii) the Forbearance Fee Payment Date (i.e., earliest of consummation of a sale/recapitalization transaction, acceleration of Obligations, and payment in full of Obligations). CIT is entitled to a forbearance fee of \$450,000 on the Forbearance Fee Payment Date. If the Forbearance Period is automatically extended, we have agreed to pay Garrison an additional 0.25% fee and CIT an additional \$125,000 fee (which, in each case, may be pro-rated for the period from October 15, 2015 until November 15, 2015, if the entire period is not needed).

As noted above, the Forbearance Agreements also provide for amendments to the revolving credit agreement and term loan credit agreement. Each Forbearance Agreement amended the definition of Availability under the respective revolving credit agreement and term loan credit agreement to reduce the minimum availability requirement to \$4,500,000 from \$7,500,000. In addition, the CIT Forbearance Agreement modified the definition of Eligible Accounts to permit as eligible accounts, until the Forbearance Termination Date (as it may be extended), trade accounts owing from Nordstrom and its affiliates not exceeding 55% of aggregate eligible accounts. After the Forbearance Termination Date (as it may be extended), the 55% applicable to Nordstrom and its affiliates will revert to 45%.

As a result of the Forbearance Agreements, while existing defaults remain under the revolving credit agreement and term loan credit agreement, Garrison and CIT and the respective lenders must forbear from the exercise of certain rights and remedies, such as the acceleration of the obligations during the Forbearance Period. The respective Forbearance Agreements contain covenants applicable during the Forbearance Period including, among others, covenants requiring compliance with a budget and provision, on a weekly basis, of reports of actual results as compared to the budget, and continuation of the engagement of Carl Marks to provide investment banking services, including execution of the sales/recapitalization process in accordance with specified milestones and restructuring advice. The sales/recapitalization process refers to the sale of substantially all of the assets or the obtaining of financing sufficient to satisfy all obligations under the respective credit agreements. The milestones relate to certain deadlines to achieve various steps in connection with a proposed merger/acquisition transaction.

On July 6, 2015, our board of directors approved and adopted Amended and Restated Bylaws, or the Amended and Restated Bylaws, which amend and restate the provisions of our existing bylaws in their entirety. The Amended and Restated Bylaws provide, among other things, that: (i) to bring any business before an annual meeting, a stockholder must give our Secretary written notice no later than the close of business on the 90th day and no earlier than the opening of business on the 120th day before the anniversary of the preceding annual stockholders meeting; provided, however, that if the annual meeting is set more than 30 days earlier or more than 60 days later than such anniversary date, notice by the stockholder must be received no earlier than the opening of business on the 120th day before the meeting and no later than the later of the close of business on the 90th day before the meeting or the close of business on the 10th day following public disclosure of the date of the annual meeting. Notwithstanding the previous sentence, for purposes of determining whether a stockholder's notice shall have been received in a timely manner for the annual meeting of stockholders in 2015, to be timely, a stockholder's notice must have been received not later than the close of business on August 15, 2015, nor earlier than the opening of business on July 15, 2015. Any stockholder proposal will be deemed to have satisfied the advance notice requirements if the stockholder has notified us of their intention to present a proposal at an annual meeting in compliance with Rule 14a-8 of the Securities Exchange Act of 1934, as amended, and such stockholder's proposal has been included in our proxy statement; (ii) any action required or permitted to be taken by our stockholders must be effected at a duly called annual or special meeting of the stockholders and may not be effected by written consent in lieu of meeting; (iii) we will, to the fullest extent permitted by law, indemnify our current and former directors and officers against all liability incurred in connection with any threatened, pending or completed proceeding; provided, however, that an eligible director or officer will be indemnified by us in connection with a proceeding initiated by such person only if the proceeding was authorized by the board; and (iv) the Court of Chancery of the State of Delaware (or, if the Court of Chancery does not have jurisdiction, the federal district court for the District of Delaware) shall be the sole and exclusive forum for certain actions brought on behalf of or against us, unless we consent in writing to an alternative forum.

Table of Contents

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

**Forward-Looking Statements**

When used in this Quarterly Report on Form 10-Q, or Quarterly Report, the words may, will, expect, anticipate, intend, estimate, continue to believe, plan, project, will be, will continue, will likely result, and similar expressions are intended to identify forward-looking statements. Similarly, statements that describe our future expectations, objectives and goals or contain projections of our future results of operations or financial condition are also forward-looking statements. Statements looking forward in time are included in this Quarterly Report pursuant to the safe harbor provision of the Private Securities Litigation Reform Act of 1995. Such statements are subject to certain risks and uncertainties, which could cause actual results to differ materially, including, without limitation, the risk that we are in default of our financing agreements entered into in connection with the acquisition of Hudson Clothing Holdings, Inc. and its subsidiaries, or collectively Hudson, and that if we are unable to secure a resolution, which could restrict our ability to operate as a going concern or cause us to become bankrupt or insolvent; the risk that we incurred substantial indebtedness to finance the acquisition of Hudson, and it may be necessary to refinance or extend our indebtedness, which may decrease our business flexibility and adversely affect our financial results; the risk that we pledged all our tangible and intangible assets as collateral under our financing agreements; the risk that our auditors have reported that there are substantial doubts as to our ability to continue as a going concern; the risk that the resignation of our president and chief executive officer, the appointment of our interim chief executive officer, and any potential search for, and appointment of, a long term chief executive officer could have a material adverse impact on our business; the risk that we are currently not in compliance with The Nasdaq Stock Market LLC's, or Nasdaq, continued listing requirements, which may cause us to be delisted; the risk that we incurred and may continue to incur significant transaction and acquisition related costs in connection with the acquisition and integration of Hudson into our business plan; the risk that our existing stockholders may be diluted if we choose to settle the convertible notes by issuing shares of our common stock; the risk that we will be unsuccessful in integrating Hudson and achieving our intended results as a result of the acquisition of Hudson; the risk that our foreign sourcing of our products and the implementation of foreign production for Hudson's products may adversely affect our business; the risk that we will be unsuccessful in gauging fashion trends and changing customer preferences; the risk that changes in general economic conditions, consumer confidence or consumer spending patterns will have a negative impact on our financial performance or strategies; the risks associated with leasing retail space and operating our own retail stores; the highly competitive nature of our business in the United States and internationally and our dependence on consumer spending patterns, which are influenced by numerous other factors; our ability to respond to the business environment and fashion trends; continued acceptance of our brands in the marketplace; our reliance on a small number of large customers; successful implementation of any growth or strategic plans; effective inventory management; the risk of cyber attacks and other system risks; our ability to continue to have access on favorable terms to sufficient sources of liquidity necessary to fund ongoing cash requirements of our operations, which access may be adversely impacted by a number of factors, including the reduced availability of credit, generally, and the substantial tightening of the credit markets, including lending by financial institutions, who are sources of credit for us, the recent increase in the cost of capital, the level of our cash flows, which will be impacted by the level of consumer spending and retailer and consumer acceptance of its products; our ability to generate positive cash flow from operations; competitive factors, including the possibility of major customers sourcing product overseas in competition with our products; the risk that acts or omissions by our third party vendors could have a negative impact on our reputation; a possible oversupply of denim in the marketplace; and the risk factors contained in our reports filed with the Securities and Exchange Commission, or SEC, pursuant to the Securities Exchange Act of 1934, as amended, or Exchange Act, including our Annual Report on Form 10-K for the year ended November 30, 2014, or Annual Report, and in Part II, Item 1A of this Quarterly Report on Form 10-Q under the heading Risk Factors. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Our future results, performance or achievements could differ materially from those expressed or implied in these forward-looking statements. We do not undertake any obligation to publicly revise these forward-looking statements to reflect events or circumstances occurring after the date hereof or to reflect the occurrence of unanticipated events, except as required by law.

**Introduction**

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This discussion and analysis summarizes the significant factors affecting our results of operations and financial conditions during the three and six month periods ended May 31, 2015 and 2014. This discussion should be read in conjunction with our Audited Consolidated Financial Statements and the related notes thereto contained in our Annual Report and our Condensed Consolidated Financial Statements, Notes to Unaudited Condensed Consolidated Financial Statements and supplemental information contained in this Quarterly Report.

Table of Contents

**Executive Overview**

Our principal business activity is the design, development and worldwide marketing of apparel products, which include denim jeans, related casual wear and accessories that bear the brands Joe s® and Hudson®. Joe s® was established in 2001 and the brand is recognized in the premium denim industry, an industry term for denim jeans with price points generally of \$120 or more, for its quality, fit and fashion-forward designs. Hudson was established in 2002, and is similarly recognized as a premier designer and marketer of women s and men s premium branded denim apparel. Because we focus on design, development and marketing, we rely on third parties to manufacture our apparel products. We sell our products through our own retail stores and to numerous retailers, which include major department stores, specialty stores and distributors around the world.

On September 30, 2013, we acquired all of the outstanding equity interests in Hudson, a designer and marketer of women s and men s premium branded denim apparel, for an aggregate purchase price consisting of approximately \$65,416,000 in cash and approximately \$27,451,000 in convertible notes, net of discount. We also issued promissory notes, bearing no interest, for approximately \$1,235,000 in aggregate principal amount that was paid on April 1, 2014 to certain option holders of Hudson. This acquisition provides us with an additional proven premium denim brand and enhances our prospects for growth across wholesale, retail and e-commerce, both domestically and overseas, and creates the potential for improved purchasing authority with current and future vendors and other operational efficiencies. As of the acquisition date, the acquired business represented approximately 40 percent of our consolidated total assets at November 30, 2013 and approximately three percent of consolidated net loss for the year ended November 30, 2013.

Our independent auditors, Moss Adams LLP, in their audit report on our annual 2014 financial statements dated February 13, 2015, have expressed their substantial doubt about our ability to continue as a going concern due to our net working capital deficiency due to debt covenant violations and our recurring losses from operations. All financial statements and information have been prepared assuming that we will continue as a going concern. While management is evaluating all options to cure the defaults, including refinancing, extending the indebtedness and exploring all other alternatives for other sources of capital for ongoing cash needs, including a sale of assets or the company, there can be no assurance that we will be able to secure a resolution or refinance or extend the indebtedness and, accordingly, our liquidity and ability to operate could be adversely affected. We have engaged Carl Marks Advisory Group to assist us as we explore all alternatives. We are currently in discussions with our creditors under both of the term loan credit agreement and revolving credit agreement regarding a resolution to the defaults, and our ability to continue as a going concern is dependent upon us resolving the outstanding indebtedness. As further described in the Subsequent Events below, we have secured a forbearance from our lenders whereby they have agreed to forbear from exercising certain of their respective rights and remedies with respect to each existing default (generally defined as existing and certain future anticipated or possible events of default) during the forbearance period. In addition, we have amended our agreements to allow for increased excess availability under the loans. Our financial statements do not include any adjustments relating to the recoverability and classification of recorded assets or the amounts and classifications of liabilities that might be necessary should we be unable to continue as a going concern.

Our Joe s® product line includes women s and men s denim jeans, pants, shirts, sweaters, jackets and other apparel products. We also offer women s handbags and clutches, women s intimates, children s products, shoes, belts and leather goods produced by us or under various license agreements and we receive royalty payments based upon net sales from licensees. Our Hudson® product line includes women s, men s and children s denim jeans, pants, jackets and other bottoms. Similar to the evolution of Joe s®, we expect to evaluate offering a range of products under the Hudson® brand name. We continue to sell our else brand in an extremely limited manner in the international market.

During the first half of fiscal 2015, our business was impacted by a decrease in overall sales in both our wholesale and retail segments. Sales of our men's and women's denim bottoms continue to be impacted by a weakening in the overall denim market, as consumer preference shifts to non-denim bottoms. Both brands have been focusing on designing new products in a variety of fits and washes with new and innovative fabrics to give the customer a reason to purchase a new pair of jeans.

In November 2014, we announced that we received an initial notice of default and event of default and demand for payment of default interest from Garrison Loan Agency Services LLC, or Garrison, as term loan agent, under the term loan facility entered into on September 30, 2013. As a result of the event of default under the term loan facility, this also triggered a default and an event of default under the terms of the revolving credit facility with CIT Commercial Services, a unit of CIT Group Inc., or CIT, entered into on September 30, 2013. As a result of such defaults and events of default, both of CIT and Garrison have reserved their respective rights to exercise any and all remedies available to them under their respective agreements and have demanded payment of interest under those agreements at the default rate of interest. In addition, as a result of the events of default under the term loan facility and the revolving credit facility, we are also in default of our subordinated convertible notes issued to the former equity owners of Hudson because we are prohibited from making any payments under the subordinated convertible notes. We are also prohibited from making any buy-out payments to Mr. Dahan. On February 10, 2015, we received additional notices of default and events of default for failure to comply with certain financial and other covenants and a demand for continued payment of default interest from both Garrison and CIT. We are currently in discussions with Garrison and CIT regarding a resolution to the defaults and events of default, including refinancing some or all of the debt and/or amendments to some or all of the existing agreements. However, there can be no assurance that we will be able to refinance or that the requested amendments will be granted on terms acceptable to us or at all. On June 26, 2015, we entered into forbearance agreements and amendments to the revolving and term loan credit agreements with Garrison and CIT. Under the terms of the forbearance, the lenders have agreed to forbear from exercising certain of their respective rights and remedies with respect to each existing default (generally defined as existing and certain future anticipated or possible events of default) for a period of time.



Table of Contents

For the remainder of 2015, we believe that our growth drivers will be dependent upon the resolution of our defaults under our term loan and revolving credit agreements with Garrison and CIT, respectively, which includes the increased excess availability under our financing agreements, integration of our operations with our Hudson brand, cost savings resulting from operational benefits or synergies of the two brands, the performance of our retail stores, continued increases from our international and men's sales, performance of our licensee's under their respective agreements for children's products, shoes and intimates and enhancement of products available to our customers. Since our retail expansion commenced in 2008, we currently operate 33 retail stores, 13 of which are full price retail stores and 20 of which are outlet stores. We did not open any new stores in fiscal 2014 and one full price retail store's lease expired in the second quarter of fiscal 2014. We do not have any signed leases for store openings in 2015 or beyond. It is necessary for us to integrate the operations of Hudson in order to reduce expenses and achieve the synergies that were expected as a result of the acquisition of Hudson.

Our business is seasonal. The majority of the marketing and sales orders take place from late fall to late spring. The greatest volume of shipments and actual sales are generally made from summer through early fall, which coincides with our third and fourth fiscal quarters, and accordingly, our cash flow is strongest in those quarters. Due to the seasonality of our business, as well as the evolution and changes in our business and product mix, including our acquisition of Hudson, our quarterly or yearly results are not necessarily indicative of the results for the next quarter or year. Furthermore, because of the growing number of full-price retail and outlet stores opened at different points during the past few fiscal years, we continue to assess the seasonality of our business on our retail segment and its potential impact on our financial results.

Our reportable business segments are Wholesale and Retail. We manage, evaluate and aggregate our operating segments for segment reporting purposes primarily on the basis of business activity and operation. Our Wholesale segment is comprised of sales of Joe's® and Hudson® products to retailers, specialty stores and international distributors, revenue from licensing agreements and includes expenses from sales, trade shows, distribution, product samples and customer service departments. Our Retail segment is comprised of sales to consumers through full-price retail stores, outlet stores and through our online retail sites at [www.joesjeans.com](http://www.joesjeans.com) and [www.hudsonjeans.com](http://www.hudsonjeans.com). Our Corporate and other is comprised of expenses from corporate operations, which include the executive, finance, legal, human resources, design and production departments and general advertising expenses associated with our products.

**Subsequent Events**

On June 26, 2015, we entered into a Forbearance and Amendment No. 3 to Revolving Credit Agreement, or the CIT Forbearance Agreement, with CIT. The CIT Forbearance Agreement requires CIT and the lenders to forbear from exercising certain of their respective rights and remedies with respect to each existing default (generally defined as existing and certain future anticipated or possible events of default) under the revolving credit agreement during the forbearance period and further amends the revolving credit agreement.

Concurrent with the CIT Forbearance Agreement, we entered into a substantially similar forbearance agreement with Garrison, or the Garrison Forbearance Agreement, that also amended the term loan credit agreement. The CIT Forbearance Agreement and Garrison Forbearance Agreement are collectively referred to as the Forbearance Agreements.

Both of the Forbearance Agreements provide that each of the lenders will forbear from exercising certain of their respective rights and remedies during the forbearance period with respect to existing defaults. The Forbearance Period ends upon the earliest to occur of a Forbearance Default or October 15, 2015, or the Forbearance Termination Date. The Forbearance Period is automatically extended until November 15, 2015 if at the

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Forbearance Termination Date no Forbearance Default has occurred and all of the milestones with respect to a sale/recapitalization process have been met, except for shareholder approval, or the Extended Forbearance Termination Date. To induce the lenders to enter into the Garrison Forbearance Agreement, we have agreed to pay a forbearance fee of 1.35 percent of the greater of the outstanding balance of the obligations under the term loan credit agreement on (i) June 26, 2015 or (ii) the Forbearance Fee Payment Date (i.e., earliest of consummation of a sale/recapitalization transaction, acceleration of Obligations, and payment in full of Obligations). CIT is entitled to a forbearance fee of \$450,000 on the Forbearance Fee Payment Date. If the Forbearance Period is automatically extended, we have agreed to pay Garrison an additional 0.25 percent fee and CIT an additional \$125,000 fee (which, in each case, may be pro-rated for the period from October 15, 2015 until November 15, 2015, if the entire period is not needed).

Table of Contents

As noted above, the Forbearance Agreements also provide for amendments to the revolving credit agreement and term loan credit agreement. Each Forbearance Agreement amended the definition of Availability under the respective revolving credit agreement and term loan credit agreement to reduce the minimum availability requirement to \$4,500,000 from \$7,500,000. In addition, the CIT Forbearance Agreement modified the definition of Eligible Accounts to permit as eligible accounts, until the Forbearance Termination Date (as it may be extended), trade accounts owing from Nordstrom's and its affiliates not exceeding 55% of aggregate eligible accounts. After the Forbearance Termination Date (as it may be extended), the 55 percent applicable to Nordstrom and its affiliates will revert to 45 percent.

As a result of the Forbearance Agreements, while existing defaults remain under the revolving credit agreement and term loan credit agreement, Garrison and CIT and the respective lenders must forbear from the exercise of certain rights and remedies, such as the acceleration of the obligations during the Forbearance Period. The respective Forbearance Agreements contain covenants applicable during the Forbearance Period including, among others, covenants requiring compliance with a budget and provision, on a weekly basis, of reports of actual results as compared to the budget, and continuation of the engagement of Carl Marks to provide investment banking services, including execution of the sales/recapitalization process in accordance with specified milestones and restructuring advice. The sales/recapitalization process refers to the sale of substantially all of the assets or the obtaining of financing sufficient to satisfy all obligations under the respective credit agreements. The milestones relate to certain deadlines to achieve various steps in connection with a proposed merger/acquisition transaction.

On July 6, 2015, our board of directors approved and adopted Amended and Restated Bylaws, or the Amended and Restated Bylaws, which amend and restate the provisions of our existing bylaws in their entirety. The Amended and Restated Bylaws provide, among other things, that: (i) to bring any business before an annual meeting, a stockholder must give our Secretary written notice no later than the close of business on the 90th day and no earlier than the opening of business on the 120th day before the anniversary of the preceding annual stockholders meeting; provided, however, that if the annual meeting is set more than 30 days earlier or more than 60 days later than such anniversary date, notice by the stockholder must be received no earlier than the opening of business on the 120th day before the meeting and no later than the later of the close of business on the 90th day before the meeting or the close of business on the 10th day following public disclosure of the date of the annual meeting. Notwithstanding the previous sentence, for purposes of determining whether a stockholder's notice shall have been received in a timely manner for the annual meeting of stockholders in 2015, to be timely, a stockholder's notice must have been received not later than the close of business on August 15, 2015, nor earlier than the opening of business on July 15, 2015. Any stockholder proposal will be deemed to have satisfied the advance notice requirements if the stockholder has notified us of their intention to present a proposal at an annual meeting in compliance with Rule 14a-8 of the Securities Exchange Act of 1934, as amended, and such stockholder's proposal has been included in our proxy statement; (ii) any action required or permitted to be taken by our stockholders must be effected at a duly called annual or special meeting of the stockholders and may not be effected by written consent in lieu of meeting; (iii) we will, to the fullest extent permitted by law, indemnify our current and former directors and officers against all liability incurred in connection with any threatened, pending or completed proceeding; provided, however, that an eligible director or officer will be indemnified by us in connection with a proceeding initiated by such person only if the proceeding was authorized by the board; and (iv) the Court of Chancery of the State of Delaware (or, if the Court of Chancery does not have jurisdiction, the federal district court for the District of Delaware) shall be the sole and exclusive forum for certain actions brought on behalf of or against us, unless we consent in writing to an alternative forum.

**Comparison of Three Months Ended May 31, 2015 to Three Months Ended May 31, 2014**

	May 31, 2015	Three months ended ( dollar values in thousands )		
		May 31, 2014	\$ Change	% Change
Net sales	\$ 47,229	\$ 48,167	\$ (938)	(2)%
Cost of goods sold	27,835	25,594	2,241	9%
Gross profit	19,394	22,573	(3,179)	(14)%
Gross margin	41%	47%		

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Selling, general & administrative	17,781	18,125	(344)	(2)%
Depreciation & amortization	996	1,160	(164)	(14)%
Operating income	617	3,288	(2,671)	(81)%
Interest expense	3,944	3,355	589	18%
Other income		(4,818)	4,818	100%
Income (loss) before provision for taxes	(3,327)	4,751	(8,078)	(170)%
Income tax expense	22	2,412	(2,390)	(99)%
<b>Net income (loss) and comprehensive income (loss)</b>	\$ (3,349)	\$ 2,339	\$ (5,688)	(243)%

Table of Contents**Three Months Ended May 31, 2015 Overview**

The following table sets forth certain statements of operations data by our reportable segments for the periods as indicated:

	Three months ended ( dollar values in thousands )				% Change
	May 31, 2015	May 31, 2014	\$ Change		
<b>Net sales:</b>					
Wholesale	\$ 39,984	\$ 40,401	\$ (417)		(1)%
Retail	7,245	7,766	(521)		(7)%
	\$ 47,229	\$ 48,167	\$ (938)		(2)%
<b>Gross profit:</b>					
Wholesale	\$ 14,307	\$ 17,218	\$ (2,911)		(17)%
Retail	5,087	5,355	(268)		(5)%
	\$ 19,394	\$ 22,573	\$ (3,179)		(14)%
<b>Operating income (loss):</b>					
Wholesale	\$ 8,394	\$ 11,560	\$ (3,166)		(27)%
Retail	99	103	(4)		(4)%
Corporate and other	(7,876)	(8,375)	499		6%
	\$ 617	\$ 3,288	\$ (2,671)		(81)%

For the three months ended May 31, 2015, or the second quarter of fiscal 2015, our net sales decreased to \$47,229,000 from \$48,167,000 for the three months ended May 31, 2014, or the second quarter fiscal 2014, a two percent decrease. We had operating income of \$617,000 compared to \$3,288,000 for the second quarter of fiscal 2014.

**Net Sales**

Our overall net sales decreased to \$47,229,000 for the second quarter of fiscal 2015 from \$48,167,000 for the second quarter of fiscal 2014, a two percent decrease. Sales of our men's and women's denim bottoms continue to be impacted by a weakening in the overall denim market, as consumer preference shifts to non-denim bottoms. Both brands have been focusing on designing new products in a variety of fits and washes with new and innovative fabrics to give the customer a reason to purchase a new pair of jeans.

More specifically, our wholesale net sales decreased to \$39,984,000 for the second quarter of fiscal 2015 from \$40,401,000 for the second quarter of fiscal 2014, a one percent decrease. This decrease in our wholesale sales is primarily attributed to a decrease in wholesale sales from Hudson® of \$563,000, or three percent, compared to the first quarter of fiscal 2014.

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Our retail net sales decreased to \$7,245,000 for the second quarter of fiscal 2015 from \$7,766,000 for the second quarter of fiscal 2014, a seven percent decrease. The primary reason for this decrease included a \$735,000 decrease in retail sales from Joe's® retail sales mostly due to lower traffic, which was partially offset by a \$214,000 increase in Hudson's® e-shop sales. Same store sales, which includes Joe's® stores opened at least 12 months and our Joe's® e-shop, decreased by 10 percent. Same store sales for our brick and mortar Joe's® stores decreased by 14 percent. Same store sales for our Joe's® e-shop increased by 27 percent and same store sales for our Hudson's® e-shop increased by 26 percent.

### Gross Profit

Our gross profit decreased to \$19,394,000 for the second quarter of fiscal 2015 from \$22,573,000 for the second quarter of fiscal 2014, a 14 percent decrease. Our overall gross margin percentage decreased to 41 percent for the second quarter of fiscal 2015 from 47 percent for the second quarter of fiscal 2014. Our overall gross margin percentage for the second quarter of fiscal 2015 was negatively impacted by an inventory write down of \$1,858,000 to the lower of cost or market for finished goods inventory as we continued to liquidate aged inventory. There were no inventory write downs in the second quarter of fiscal 2014.

Our wholesale gross profit decreased to \$14,307,000 for the second quarter of fiscal 2015 from \$17,218,000 for the second quarter of fiscal 2014, a 17 percent decrease. Our wholesale gross profit decreased for the second quarter of fiscal 2015 compared to the second quarter of fiscal 2014 due to lower wholesale sales, additional inventory write down for finished goods and liquidation sales related to aged inventory. Our wholesale gross margin percentage for the second quarter of fiscal 2015 decreased to 36 percent compared to 43 percent for the prior year comparable period. The decrease in gross margin percentage is mostly attributed to additional inventory write down for finished goods, as we continue to monitor and make adjustments, as necessary and liquidation sales related to aged inventory.

Table of Contents

Our retail gross profit decreased to \$5,087,000 for the second quarter of fiscal 2015 from \$5,355,000 for the second quarter of fiscal 2014, a five percent decrease. Our gross margin percentage was 70 percent for the second quarter of fiscal 2015 compared to 69 percent for the second quarter of fiscal 2014, and increased due to less promotional activity at our retail stores than the prior year comparable period.

**Selling, General and Administrative Expense, including Depreciation and Amortization**

Selling, general and administrative, or SG&A, expenses, including depreciation and amortization, decreased to \$18,777,000 for the second quarter of fiscal 2015 from \$19,285,000 for the second quarter of fiscal 2014, a three percent decrease. Our SG&A expenses were impacted by additional fees of \$1,061,000 in connection with investment banking, restructuring and legal advice related to the evaluation of our strategic alternatives in connection with the default under our term loan and revolving credit agreements. Our SG&A includes expenses related to employee and employee related benefits, sales commissions, contingent consideration expense, advertising, sample production, facilities and distribution related costs, professional fees, stock-based compensation, factor and bank fees, fees associated with the evaluation of our strategic alternatives related to the default under our term loan and revolving credit agreements, expenses related to Hudson's operation as our subsidiary and also includes depreciation and amortization.

Our wholesale SG&A expense increased to \$5,913,000 for the second quarter of fiscal 2015 from \$5,658,000 for the second quarter of fiscal 2014, or a five percent increase. Our wholesale SG&A expense was slightly higher in the second quarter of fiscal 2015 mostly due to a reserve for bad debt expense for Hudson associated with one of its international distributors.

Our retail SG&A expense decreased to \$4,988,000 for the second quarter of fiscal 2015 from \$5,252,000 for the second quarter of fiscal 2014, a five percent decrease. Our retail SG&A expense decreased mostly due to lower salary and operating supply costs.

Our corporate and other SG&A expense decreased to \$7,876,000 for the second quarter of fiscal 2015 from \$8,375,000 for the second quarter of fiscal 2014, a six percent decrease. Our corporate and other SG&A expense includes general overhead associated with our operations, including Hudson. Our decrease in SG&A expenses was attributable to lower corporate operating expenses, which were mostly offset by additional fees of \$1,061,000 in connection with investment banking, restructuring and legal advice related to strategic alternatives in connection with the default under our term loan and revolving credit agreements.

**Operating Income (Loss)**

We had operating income of \$617,000 for the second quarter of fiscal 2015 compared to \$3,288,000 for the second quarter of fiscal 2014. Our decrease in operating income was primarily due to lower wholesale sales and gross profit as discussed above.

Our wholesale operating income decreased to \$8,394,000 in the second quarter of fiscal 2015 from \$11,560,000 for the second quarter of fiscal 2014, a 27 percent decrease. We had retail operating income of \$99,000 in the second quarter of fiscal 2015 compared to \$103,000 in the second quarter of fiscal 2014. Corporate operating loss decreased to \$7,876,000 for the second quarter of fiscal 2015 from \$8,375,000 for the second quarter of fiscal 2014.

**Interest Expense**

Our interest expense increased to \$3,944,000 for the second quarter of fiscal 2015 from \$3,355,000 for the second quarter of fiscal 2014. Our interest expense is primarily associated with interest expense from our revolving and term loan credit agreements with CIT and Garrison, interest expense and PIK interest from our convertible notes and amortization of debt discounts and deferred financing costs associated with the finance arrangements resulting from the Hudson acquisition. Effective retroactively to October 1, 2014, we began paying additional interest to both CIT and Garrison, respectively, due to the default under the respective agreements. We pay to CIT an additional two percent interest and to Garrison an additional two percent interest.

**Other Income**

Other income represents the benefit due to the change in fair value of the embedded conversion derivative from February 28, 2014 to May 8, 2014 of \$4,818,000.



Table of Contents**Income Tax**

Our effective tax rate was an expense of negative one percent for the second quarter of fiscal 2015 compared to 51 percent for the second quarter of fiscal 2014. The decreased effective tax rate for the second quarter of fiscal 2015 resulted from our loss before provision for taxes being subject to a valuation allowance. Differences between our annualized effective tax rate and statutory tax rate are primarily due to state taxes and the valuation allowance.

**Net (Loss) Income and Comprehensive (Loss) Income**

We generated a net loss of \$3,349,000 for the second quarter of fiscal 2015 compared to net income of \$2,339,000 for the second quarter of fiscal 2014.

**Comparison of Six Months Ended May 31, 2015 to Six Months Ended May 31, 2014**

	May 31, 2015	Six months ended (dollar values in thousands)		% Change
		May 31, 2014	\$ Change	
Net sales	\$ 90,246	\$ 95,511	\$ (5,265)	(6)%
Cost of goods sold	52,753	51,453	1,300	3%
Gross profit	37,493	44,058	(6,565)	(15)%
Gross margin	42%	46%		
Selling, general & administrative	38,102	37,077	1,025	3%
Depreciation & amortization	2,008	2,387	(379)	(16)%
Operating income (loss)	(2,617)	4,594	(7,211)	(157)%
Interest expense	7,828	6,676	1,152	17%
Other income		(2,268)	2,268	100%
Income (loss) before provision for taxes	(10,445)	186	(10,631)	(5,716)%
Income tax expense	14,499	25	14,474	57,896%
<b>Net income (loss) and comprehensive income (loss)</b>	<b>\$ (24,944)</b>	<b>\$ 161</b>	<b>\$ (25,105)</b>	<b>(15,593)%</b>

Table of Contents**Six Months Ended May 31, 2015 Overview**

The following table sets forth certain statements of operations data by our reportable segments for the periods as indicated:

	Six months ended ( dollar values in thousands )			
	May 31, 2015	May 31, 2014	\$ Change	% Change
<b>Net sales:</b>				
Wholesale	\$ 75,445	\$ 80,016	\$ (4,571)	(6)%
Retail	14,801	15,495	(694)	(4)%
	\$ 90,246	\$ 95,511	\$ (5,265)	(6)%
<b>Gross profit:</b>				
Wholesale	\$ 27,582	\$ 33,978	\$ (6,396)	(19)%
Retail	9,911	10,080	(169)	(2)%
	\$ 37,493	\$ 44,058	\$ (6,565)	(15)%
<b>Operating income (loss):</b>				
Wholesale	\$ 16,186	\$ 21,931	\$ (5,745)	(26)%
Retail	(508)	(885)	377	43%
Corporate and other	(18,295)	(16,452)	(1,843)	(11)%
	\$ (2,617)	\$ 4,594	\$ (7,211)	(157)%

For the six months ended May 31, 2015, our net sales decreased to \$90,246,000 from \$95,511,000 for the six months ended May 31, 2014, a six percent decrease. We had an operating loss of \$2,617,000 for the six months ended May 31, 2015 compared to operating income of \$4,594,000 for the six months ended May 31, 2014.

**Net Sales**

Our net sales decreased to \$90,246,000 for the six months ended May 31, 2015 from \$95,511,000 for the six months ended May 31, 2014, a six percent decrease.

More specifically, our wholesale net sales decreased to \$75,445,000 for the six months ended May 31, 2015 compared to \$80,016,000 for the six months ended May 31, 2014, a six percent decrease. This decrease in our wholesale sales is primarily attributed to a decrease in both our domestic men's and women's wholesale and international sales. The decreases were partially offset by a \$613,000 increase in sales from our else brand, as we continued to sell some of our inventory internationally. We continue to believe that the future of the else brand is limited.

Our retail net sales decreased to \$14,801,000 for the six months ended May 31, 2015 compared to \$15,495,000 for the six months ended May 31, 2014, a four percent decrease. The primary reason for this decrease included a \$778,000 decrease in retail sales from Joe's® retail sales,

which was partially offset by an \$84,000 increase in Hudson® e-shop sales. Same store sales, which includes Joe's® stores opened at least 12 months and our Joe's® e-shop, decreased by four percent. Same store sales for our brick and mortar Joe's® stores decreased by eight percent. Same store sales for our Joe's® e-shop increased by 22 percent and same store sales for our Hudson® e-shop increased by four percent.

**Gross Profit**

Our gross profit decreased to \$37,493,000 for the six months ended May 31, 2015 compared to \$44,058,000 for the six months ended May 31, 2014, a 15 percent decrease. Our overall gross margin was 42 percent for the six months ended May 31, 2015 compared to 46 percent for the six months ended May 31, 2014.

Our wholesale gross profit decreased to \$27,582,000 for the six months ended May 31, 2015 compared to \$33,978,000 for the six months ended May 31, 2014, a 19 percent decrease. Our wholesale gross profit decreased for the six months ended May 31, 2015 compared to the six months ended May 31, 2014 due to lower wholesale sales, \$2,723,000 of additional inventory write down for finished goods and fabric, and liquidation sales related to aged inventory. Our wholesale gross margin percentage for the six months ended May 31, 2015 decreased to 37 percent compared to 43 percent for the prior year comparable period. The decrease in gross margin percentage is mostly attributed to additional inventory write down for finished goods and fabric, as we continue to monitor and make adjustments, as necessary, and liquidation sales related to aged inventory.

Table of Contents

Our retail gross profit decreased to \$9,911,000 for the six months ended May 31, 2015 compared to \$10,080,000 for the six months ended May 31, 2014, a two percent decrease. Our gross margin percentage was 67 percent for the six months ended May 31, 2015 compared to 65 percent for the six months ended May 31, 2014, and increased primarily due to less promotional activity in our retail stores than during the prior year comparative period.

**Selling, General and Administrative Expense, including Depreciation and Amortization**

SG&A expenses increased to \$40,110,000 for the six months ended May 31, 2015 compared to \$39,464,000 for the six months ended May 31, 2014, a two percent increase. Our SG&A expenses increase was attributable to additional fees in connection with investment banking, restructuring and legal advice related to the evaluation of our strategic alternatives in connection with the default under our term loan and revolving credit agreements. Our SG&A includes expenses related to employee and employee related benefits, sales commissions, contingent consideration expense, advertising, sample production, facilities and distribution related costs, professional fees, stock-based compensation, factor and bank fees, fees associated with the evaluation of our strategic alternatives related to the default under our term loan and revolving credit agreements, expenses related to Hudson's operation as our subsidiary and also includes depreciation and amortization. Due to these additional expenses, our SG&A expenses increased correspondingly for the six months ended May 31, 2015.

Our wholesale SG&A expense decreased to \$11,396,000 for the six months ended May 31, 2015 compared to \$12,047,000 for the six months ended May 31, 2014, a five percent decrease. Our wholesale SG&A expense was lower in the six months ended May 31, 2015 mostly due to lower sample, commission, employee costs and depreciation expense, which were partially offset by a reserve for bad debt expense for Hudson® associated with one of its international distributors.

Our retail SG&A expense decreased to \$10,419,000 for the six months ended May 31, 2015 compared to \$10,965,000 for the six months ended May 31, 2014, a five percent decrease. Our retail SG&A expense decreased mostly due to the costs associated with operating one less store between the end of the six months ended May 31, 2014 and the end of six months ended May 31, 2015, which included additional store payroll, store rents and depreciation expense.

Our corporate and other SG&A expense increased to \$18,295,000 for the six months ended May 31, 2015 compared to \$16,452,000 for the six months ended May 31, 2014, an 11 percent increase. Our corporate and other SG&A expense includes general overhead associated with our operations, including Hudson. Our increase in SG&A expenses was attributable to additional fees of \$2,819,000 associated with the separation and consulting agreement with our former President and Chief Executive Officer, the severance agreement with the President of our Hudson subsidiary and additional fees in connection with investment banking, restructuring and legal advice related to strategic alternatives in connection with the default under our term loan and revolving credit agreements.

**Operating (Loss) Income**

We had an operating loss of \$2,617,000 for the six months ended May 31, 2015 compared to operating income \$4,594,000 for the six months ended May 31, 2014. Our shift to an operating loss from operating income was primarily due to lower wholesale sales and gross profit and additional corporate operating expenses as discussed above.

Our wholesale operating income decreased to \$16,186,000 for the six months ended May 31, 2015 from \$21,931,000 in the six months ended May 31, 2014, a 26 percent decrease. We generated a retail operating loss of \$508,000 for the six months ended May 31, 2015 compared to \$885,000 in the six months ended May 31, 2014. Corporate operating loss increased to \$18,295,000 for the six months ended May 31, 2015 from \$16,452,000 for the six months ended May 31, 2014.

### **Interest Expense**

Our interest expense increased to \$7,828,000 for the six months ended May 31, 2015 from \$6,676,000 for the six months ended May 31, 2014. Our interest expense is primarily associated with interest expense from our revolving and term loan credit agreements with CIT and Garrison, interest expense and PIK interest from our convertible notes and amortization of debt discounts and deferred financing costs associated with the finance arrangements resulting from the Hudson acquisition. Effective retroactively to October 1, 2014, we began paying additional interest to both CIT and Garrison, respectively, due to the default under the respective agreements. We pay to CIT an additional two percent interest and to Garrison an additional two percent interest.

Table of Contents

**Other Income**

Other income represents the income due to the change in fair value of the embedded conversion derivative from November 30, 2014 to May 31, 2014 of \$2,268,000 for the six months ended May 31, 2014.

**Income Tax**

Our effective tax rate was an expense of negative 139 percent for the six months ended May 31, 2015 compared to 14 percent for the six months ended May 31, 2014. The decreased effective tax rate for the six months ended May 31, 2015 resulted from the discrete adjustment related to the valuation allowance that was recognized during the first quarter. Differences between our annualized effective tax rate and statutory tax rate are primarily due to state taxes and the valuation allowance. For the first quarter of fiscal 2015, the valuation allowance associated with deferred taxes as of November 30, 2014, increased by \$14,481,000. We considered all available evidence, both positive and negative, in our assessment of the valuation allowance needed as of February 28, 2015. Due to a review of operating performance for the quarter and a change in business strategy, which included the disposal of certain assets that have a fair value in excess of tax basis, we increased our valuation allowance by \$14,481,000 as of February 28, 2015.

**Net (Loss) Income and Comprehensive (Loss) Income**

Our net loss was \$24,944,000 for the six months ended May 31, 2015 compared to net income of \$161,000 for the six months ended May 31, 2014.

**Liquidity and Capital Resources**

Until the acquisition of Hudson on September 30, 2013, our primary sources of liquidity were: (i) cash from sales of our products; (ii) sales from accounts receivable factoring facilities and advances against inventory; and (iii) utilizing existing cash balances. Beginning September 30, 2013, in connection with the acquisition of Hudson, we entered into an amended and restated accounts receivable factoring facility and revolving credit agreement with CIT that provided advances to us for eligible accounts receivable and eligible inventory up to \$50,000,000, based upon the value of the eligible accounts receivable and inventory less any reserves imposed by CIT. The initial proceeds from the advances under this revolving credit facility, which included accounts receivable and inventory borrowing, were used to pay a portion of the consideration for the acquisition and fees and expenses associated with the acquisition and the remainder was used to repay our existing factor loans and for working capital and other general corporate purposes. The revolving credit facility matures on September 30, 2018 unless terminated by payment in full earlier. In addition, we entered into a term loan credit agreement for \$60,000,000 with Garrison to finance the remainder of the purchase price required for the acquisition. Under the term loan credit agreement, we pay interest to Garrison and are required to make prepayments under certain circumstances. The term loan matures on September 30, 2018. Both of these agreements, along with the convertible notes issued in connection with the acquisition are discussed in more detail below under Financing Arrangements Related to the Acquisition of Hudson.

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For the six months ended May 31, 2015, we generated \$10,841,000 of cash flow from operations mostly from the collection of receivables. Cash flow used in financing activities consisted of \$10,518,000 of repayments under our revolving credit facility. We made payments of \$51,000 for taxes on restricted stock units and we purchased \$117,000 in restricted stock. We used \$381,000 in investing activities for the purchase of property and equipment. Our cash balance decreased to \$828,000 as of May 31, 2015.

Under the amended and restated factoring agreement entered into on September 30, 2013, we continue to sell or assign to CIT certain of our accounts receivable, including accounts arising from or related to sales of inventory and the rendition of services. We pay a factoring rate of 0.50 percent for accounts for which CIT bears the credit risk, subject to discretionary surcharges and 0.35 percent for accounts for which we bear the credit risk, but in no event less than \$3.50 per invoice. The interest rate associated with borrowings equals the interest rate then in effect for Revolving A Loans pursuant to the revolving credit agreement. As of May 31, 2015, that interest rate was approximately 2.75 percent. The amended and restated factoring agreement may be terminated by CIT upon 60 days written notice or immediately upon the occurrence of an event of default as defined in the agreement. The accounts receivable agreement may be terminated by us upon 60 days written notice prior to September 30, 2018 or annually with 60 days written notice prior to September 30th of each year thereafter and remains effective until terminated.

As of May 31, 2015, our cash balance was \$828,000 and our borrowing base cash availability with CIT was approximately \$11,500,000. This amount with CIT fluctuates on a daily basis based upon invoicing and collection related activity by CIT on our behalf. As of May 31, 2015, our revolving credit facility had a balance of \$20,820,000.

Table of Contents

For the remainder of fiscal 2015, our primary capital needs are for: (i) operating expenses; (ii) payments, including interest and additional interest at the default rates, required to be made under our amended and restated factoring facility, revolving credit agreement, term loan credit agreement and convertible notes; (iii) working capital necessary to fund inventory purchases; (iv) capital expenditures to support integration costs with Hudson; (v) payments related to restructuring and advice of our financial and legal advisors related to strategic alternatives; (vi) financing extensions of trade credit to our customers; (vii) payment for the fixed amount paid to Mr. Dahan pursuant to our agreement with him, including any additional payments not made during the period we were prohibited from making payments; and (viii) payments for expenses associated with the integration of Hudson into one facility and one consolidated company with operating divisions. We anticipate funding our operations through working capital generated by the following: (i) cash flow from sales of our products from the combined companies; (ii) managing our operating expenses and inventory levels; (iii) maximizing trade payables with our domestic and international suppliers; (iv) increasing collection efforts on existing accounts receivables; and (v) utilizing our revolving credit agreement with CIT, which includes the amended and restated factoring facility.

Based on our cash on hand, cash flow from operations and the expected borrowing availability under the revolving credit agreement with CIT based upon our borrowing base and sales forecasts and assuming Garrison and CIT do not exercise any and all remedies available to them under their respective agreements due to the default, including demanding repayment of all principal and interest due under the respective agreements, we believe that we have the working capital resources necessary to meet our projected operational needs for the remainder of fiscal 2015. However, if Garrison or CIT demand repayment of all principal and interest due under their respective agreements, if we require more capital for growth and integration or if we experience a decline in sales and/or operating losses, we believe that it will be necessary to obtain additional working capital through additional credit arrangements. However, there can be no assurance that other financings will be available if needed. Our inability to fulfill any interim working capital requirements raises a substantial doubt about our ability to continue as a going concern for a reasonable period of time.

We believe that the rate of inflation over the past few years has not had a significant adverse impact on our net sales or income from continuing operations.

*Financing Arrangements Related to the Acquisition of Hudson*

As discussed above, in connection with the acquisition of Hudson we entered into a revolving credit agreement with CIT and a term loan credit agreement with Garrison. We also issued approximately \$32,445,000 in convertible notes (face amount) and promissory notes, bearing no interest, for approximately \$1,235,000 in aggregate principal amount that was paid on April 1, 2014 to certain option holders of Hudson.

The convertible notes were issued with different interest rates and conversion features for Hudson's management stockholders and Fireman Capital CPF Hudson Co-Invest LP, or Fireman, respectively. Interest on the convertible notes is paid in a combination of cash and additional paid-in-kind notes, or PIK notes. Convertible notes in an aggregate principal amount of approximately \$22,885,000 (face amount) were issued to Hudson's management stockholders, are structurally and contractually subordinated to our senior debt and mature on March 31, 2019. All of the notes are expressly junior and subordinated in right of payment to all amounts due and owing upon any indebtedness outstanding under the revolving credit facility and the term loan facility (as discussed below). Due to the defaults and events of default under the revolving credit facility and term loan facility, we are prohibited from making any payments under the subordinated convertible notes.

The management notes accrue interest quarterly on the outstanding principal amount (i) from September 30, 2013 until the earlier to occur of the date of conversion of the notes or November 30, 2014 at a rate of 10 percent per annum, which is payable 7.68 percent in cash and 2.32 percent in PIK notes, (ii) from December 1, 2014 until the earlier to occur of the date of conversion of the notes or September 30, 2016 at a rate of



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10 percent per annum payable in cash, and (iii) from October 1, 2016 until the earlier to occur of the date of conversion of the notes or the date such principal amount is paid in full at a rate of 10.928 percent per annum payable in cash. Payment of interest at the cash pay rate under clause (ii) or (iii), as applicable, for any payment date will be subject to satisfaction of certain financial conditions for us. As of December 1, 2014, we did not meet such financial conditions, and therefore, the interest continues to accrue quarterly at a rate of 10 percent per annum, which is payable 7.68 percent in cash and 2.32 percent in PIK notes. In addition, because we are prohibited from making any payments under the subordinated convertible notes, as of January 1, 2015, we began to accrue an additional two percent interest under the default rate in cash. The management notes become convertible by each of the holders beginning on September 30, 2015 until maturity on March 31, 2019 into shares of our common stock, cash, or a combination of cash and common stock, with the settlement choice at our election.

The approximately \$9,560,000 (face amount) in aggregate principal amount of convertible notes issued to Fireman are structurally and contractually subordinated to our senior debt and mature on March 31, 2019. The Fireman note accrues interest quarterly on the outstanding principal amount (i) from September 30, 2013 until the earlier to occur of the date of conversion of the notes or November 30, 2014 at a rate of 6.5 percent per annum, which is payable 3 percent in cash and 3.5 percent in PIK notes,

Table of Contents

(ii) from December 1, 2014 until the earlier to occur of the date of conversion of the notes or September 30, 2016 at a rate of 6.5 percent per annum payable in cash, and (iii) from October 1, 2016 until the earlier to occur of the date of conversion of the notes or the date such principal amount is paid in full at a rate of 7 percent per annum payable in cash. Payment of interest at the cash pay rate under clause (ii) or (iii), as applicable, for any payment date will be subject to satisfaction of certain financial conditions for us. As of December 1, 2014, we did not meet such financial conditions, and therefore, the interest continues to accrue quarterly at a rate of 6.5 percent per annum, which is payable 3 percent in cash and 3.5 percent in PIK notes. In addition, because we are prohibited from making any payments under the subordinated convertible notes, as of January 1, 2015, we accrue an additional two and a half percent interest under the default rate in cash. The Fireman note became convertible by the holder on October 14, 2014 until maturity on March 31, 2019 into shares of common stock, cash, or a combination of cash and common stock, with the settlement choice at our election.

Each of the notes is convertible, in whole but not in part, at a conversion price of \$1.78 per share, subject to certain adjustments, into approximately 18,200,000 shares of our common stock. The Fireman note may be converted at its sole election and the management notes may be converted at either a majority of the holders' election or individually, depending on the holder. If we elect to pay cash with respect to a conversion of the notes, the amount of cash to be paid per share will be equal to (a) the number of shares of common stock issuable upon such conversion multiplied by (b) the average of the closing prices for the common stock over the 20 trading day period immediately preceding the notice of conversion. We will have the right to prepay all or any portion of the principal amount of the notes at any time by paying 103 percent of the principal amount of the portion of any management note subject to prepayment or 100 percent of the principal amount of the portion of the Fireman note subject to prepayment.

In connection with the quarterly interest payments payable on January 1, 2014, April 1, 2014, July 1, 2014, October 1, 2014, January 1, 2015 and April 1, 2015 we issued a total of approximately \$218,000, \$215,000, \$219,000, \$223,000, \$225,000 and \$221,000, respectively, in the aggregate principal amount of convertible notes as PIK Notes to the holders of the convertible notes. In addition, because we are prohibited from making any payments under the subordinated convertible notes, we did not pay the quarterly interest payment on January 1, 2015 and are accruing at an additional two or two and one-half percent interest under the default rate of the agreements, respectively.

*Revolving Credit Agreement*

The revolving credit agreement with CIT provides us with a revolving credit facility up to \$50,000,000 comprised of a revolving A-1 commitment of up to \$1,000,000 and a revolving A commitment of up to \$50,000,000 minus the revolving A-1 commitment. Our actual maximum credit availability under the revolving facility varies from time to time and is determined by calculating a borrowing base, which is based on the value of the eligible accounts and eligible inventory minus reserves imposed by CIT. The revolving facility also provides for swingline loans, up to \$5,000,000 sublimit, and letters of credit, up to \$1,000,000 sublimit. Proceeds from advances under the revolving facility may be used for working capital needs and general corporate purposes and were initially used to pay a portion of the consideration for the acquisition and fees and expenses associated with the acquisition and to repay our existing factor loans.

All unpaid loans under the revolving facility mature on September 30, 2018. We have the right at any time and from time to time to terminate the commitments under the revolving facility by paying in full or prepay any borrowings, in whole or in part, without terminating or reducing the commitment. If we terminate the revolving facility in full prior to the second anniversary of the closing date, we are required to pay a prepayment fee of 1 percent or 0.5 percent of the commitments terminated depending on when we make the prepayment.

The revolving facility is guaranteed by us and all of our subsidiaries, and secured by liens on substantially all assets owned by us, including a first- priority lien on certain property, including principally trade accounts, inventory, certain related assets and proceeds of the foregoing,

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subject to permitted liens and exceptions, and a second-priority lien on all other assets, including intellectual property owned by us, which secures the term loan facility on a first-priority basis.

Advances under the revolving facility are in the form of either base rate loans or LIBOR rate loans. The interest rate for base rate loans under the revolving A commitment fluctuates and is equal to (x) the Alternate Base Rate, which is the greatest of (a) the JPMorgan Chase Bank prime rate; (b) the Federal funds rate plus 0.50 percent; and (c) the 90 day LIBO Rate, which is the rate per annum equal to the 90-Day LIBO Rate published in the New York City edition of the Wall Street Journal under Money Rates, plus 1 percent, in each case, plus (y) 1.5 percent. The interest rate for LIBOR rate loans under the revolving A commitment is equal to the 90-Day LIBO Rate per annum plus 2.5 percent. The interest rate for base rate loans and LIBOR rate loans under the revolving A-1 commitment is equal to (i) the Alternate Base Rate plus 2.5 percent and (ii) the 90-Day LIBO Rate plus 3.5 percent, respectively. Interest on the revolving facility is payable on the first day of each calendar month and the maturity date. Among other fees, we pay a commitment fee of 0.25 percent per annum (due quarterly) on the average daily amount of the unused revolving commitment under the revolving facility. We also pay fees with respect to any letters of credit. In addition, because we are in default under the revolving credit facility, we are paying an additional one percent interest under the default rate. Our average interest rate, including the default rate, is approximately 3.5 percent.

Table of Contents

The revolving credit facility contains usual and customary negative covenants for transactions of this type, including, but not limited to: restrictions on our ability and our subsidiaries' ability to create or incur indebtedness; create liens; consolidate, merge, liquidate or dissolve; sell, lease or otherwise transfer any of its assets; substantially change the nature of its business; make investments or acquisitions; pay dividends; enter into transactions with affiliates; amend material documents, prepay certain indebtedness and make capital expenditures. The negative covenants are subject to certain exceptions as specified in the revolving credit agreement.

In addition, the revolving credit agreement requires us to (a) maintain (i) at all times availability under the revolving facility of not less than \$5,000,000 and (ii) at all times the sum of availability under the revolving facility plus up to \$2,500,000 of unrestricted cash of not less than \$7,500,000; and (b) maintain a minimum fixed charge coverage ratio calculated for each four fiscal quarter period at levels set forth in the revolving facility.

As of May 31, 2015, we were not in compliance with the covenants under the revolving credit agreement as a result of an event of default under the term loan credit agreement. As of November 30, 2014 and February 28, 2015, we were out of compliance with (i) the minimum fixed charge coverage ratio of 1.09x; (ii) the covenant to timely deliver the financial plan and forecast for 2015; and (iii) the minimum fixed charge coverage ratio of 1.15x. As of May 31, 2015, we were out of compliance with the minimum fixed charge coverage ratio of 1.20x.

See *Subsequent Events* above for a discussion of the forbearance agreements and amendments to the revolving credit and term loan credit agreements entered into with CIT and Garrison.

*Term Loan Credit Agreement*

The term loan credit agreement entered into with Garrison provided for term loans of up to \$60,000,000 and was fully funded to us as of September 30, 2013. The term loan proceeds were used to finance a portion of the consideration for the acquisition of Hudson and to pay fees and expenses associated with the acquisition.

The term loan matures on September 30, 2018. We are allowed to prepay the term loan at any time, in whole or in part, subject to the payment of a prepayment fee if we prepay prior to September 30, 2016. The prepayment fee is 3 percent if we prepaid prior to September 30, 2014 and is reduced by 1 percent per year until September 30, 2016. In addition, we are required to make prepayments out of extraordinary receipts, certain percentage of the excess cash flow and certain net proceeds of certain asset sales or equity issuances, in each case (other than a prepayment in connection with excess cash flow), subject to the payment of the prepayment fee as set forth above.

The term loan facility is guaranteed by us and all of our subsidiaries, and is secured by liens on substantially all assets owned by us, including a first- priority lien on intellectual property owned by us and a second-priority lien on the revolving credit priority collateral.

The interest rate for the term loan fluctuates and is equal to the rate per annum equal to the British Banker Association Interest Settlement Rate for deposits in Dollars with a term of three months, as appears on the Bloomberg BBAM Screen, plus 10.75 percent. Interest is payable on the first day of each calendar month and the maturity date. In addition, because we are in default under the term loan agreement, we are paying an

additional two percent interest under the default rate. Our average interest rate, including the default rate, is approximately 14 percent.

The term loan credit agreement contains usual and customary negative covenants for transactions of this type, including, but not limited to: restrictions on our ability and our subsidiaries' ability to create or incur indebtedness; create liens; consolidate, merge, liquidate or dissolve; sell, lease or otherwise transfer any of its assets; substantially change the nature of its business; make investments or acquisitions; pay dividends; enter into transactions with affiliates; amend material documents, prepay certain indebtedness and make capital expenditures. The negative covenants are subject to certain exceptions as specified in the term loan credit agreement.

In addition, the term loan credit agreement also requires us to maintain (a) (i) at all times, availability under the revolving credit facility of not less than \$5,000,000 and (ii) at all times as tested on each date that a borrowing certificate is delivered, the sum of availability under the revolving credit facility plus up to \$2,500,000 of unrestricted cash of not less than \$7,500,000; (b) a minimum fixed charge coverage ratio; (c) a minimum EBITDA; and (d) a leverage ratio not more than the maximum leverage coverage ratio as set forth in the term loan credit agreement.

Table of Contents

As of May 31, 2015, we were not compliance with the covenants under the term loan credit agreement. Under the term loan credit agreement, an event of default has occurred. The minimum EBITDA for the twelve fiscal months ending (i) September 30, 2014 of \$22,136,300; (ii) October 31, 2014 of \$22,991,900; (iii) November 30, 2014 of \$23,417,800 were not met; and (iv) the financial plan and forecast for 2015 was not timely delivered. In addition, as of November 30, 2014 and February 28, 2015, we were out of compliance with the (i) minimum fixed charge coverage ratio of 1.09x; (ii) maximum leverage ratio of 3.21x; (iii) minimum fixed charge coverage ratio of 1.15x; and (iv) maximum leverage ratio of 3.00x. As of May 31, 2015, we were also out of compliance with the (i) minimum fixed charge coverage ratio of 1.20x and (ii) maximum leverage ratio of 2.75x.

See **Subsequent Events** above for a discussion of the forbearance agreements and amendments to the revolving credit and term loan credit agreements entered into with CIT and Garrison.

*Off Balance Sheet Arrangements*

We do not have any off balance sheet arrangements.

**Management's Discussion of Critical Accounting Policies**

We believe that the accounting policies discussed below are important to an understanding of our financial statements because they require management to exercise judgment and estimate the effects of uncertain matters in the preparation and reporting of financial results. Accordingly, we caution that these policies and the judgments and estimates they involve are subject to revision and adjustment in the future. While they involve less judgment, management believes that the other accounting policies discussed in **Notes to Consolidated Financial Statements - Note 2 Summary of Significant Accounting Policies** included in our Annual Report previously filed with the SEC are also important to an understanding of our financial statements. We believe that the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

*Revenue Recognition*

Wholesale revenues are recorded on the accrual basis of accounting when title transfers to the customer, which is typically at the shipping point. We record estimated reductions to revenue for customer programs, including co-op advertising, other advertising programs or allowances, based upon a percentage of sales. We also allow for returns based upon pre-approval or in the case of damaged goods. Such returns are estimated based on historical experience and an allowance is provided at the time of sale.

Retail store revenue is recognized net of estimated returns at the time of sale to consumers. E-commerce sales of products ordered through our retail internet site known as [www.joesjeans.com](http://www.joesjeans.com) are recognized upon estimated delivery and receipt of the shipment by the customers. E-commerce revenue is also reduced by an estimate of returns. Retail store revenue and E-commerce revenue exclude sales taxes. Revenue from licensing arrangements are recognized when earned in accordance with the terms of the underlying agreements, generally based upon the higher of (a) contractually guaranteed minimum royalty levels and (b) estimates of sales and royalty data received from our licensees. Payments

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received in consideration of the grant of a license or advanced royalty payments are recognized ratably as revenue over the term of the license agreement. The revenue recognized ratably over the term of the license agreement will not exceed royalty payments received. The unrecognized portion of the upfront payments are included in deferred royalties and accrued expenses depending on the long or short term nature of the payments to be recognized. As of May 31, 2015, we have recognized all of the advanced payments under our licensing agreements as income.

### *Factored Accounts and Receivables, Allowance for Customer Credits and Doubtful Allowances*

We evaluate our ability to collect on accounts receivable and charge-backs (disputes from the customer) based upon a combination of factors. Whether a receivable is past due is based on how recently payments have been received and in certain circumstances where we are aware of a specific customer's inability to meet its financial obligations (e.g., bankruptcy filings, substantial downgrading of credit sources). A specific reserve for bad debts is taken against amounts due to reduce the net recognized receivable to the amount reasonably expected to be collected. Amounts are charged off against the reserve once it is established that amounts are not likely to be collected. We recognize reserves for charge-backs based on our historical collection experience.

The balance in the allowance for customer credits and doubtful accounts as of May 31, 2015 and November 30, 2014 was \$2,099,000 and \$1,676,000, respectively, for non-factored accounts receivables.

Table of Contents

*Inventory*

We continually evaluate the composition of our inventories by assessing slow-turning, ongoing product as well as product from prior seasons. Market value of distressed inventory is valued based on historical sales trends on our individual product lines, the impact of market trends and economic conditions, and the value of current orders relating to the future sales of this type of inventory. Significant changes in market values could cause us to record additional inventory markdowns.

*Valuation of Long-lived and Intangible Assets and Goodwill*

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

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

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

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



stores.

Business acquisitions are accounted for under the purchase method by assigning the purchase price to tangible and intangible assets acquired and liabilities assumed. Assets acquired and liabilities assumed are recorded at their fair values and the excess of the purchase price over the amounts assigned is recorded as goodwill. Purchased intangible assets with finite lives are amortized over their estimated useful lives. Goodwill and intangible assets with indefinite lives are not amortized but are tested at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable for impairment.

In fiscal 2007, we acquired through merger JD Holdings, which included all of the goodwill and intangible assets goodwill related to the Joe s®, Joe s Jeans and JD® logo and marks. On September 30, 2013, we acquired Hudson, which included all of the goodwill and intangible assets related to the Hudson® logos and marks. We have assigned an indefinite life to the remaining intangible assets relating to the trademarks acquired, and therefore, no amortization expenses are expected to be recognized. However, we will test the assets for impairment annually in accordance with our critical accounting policies.

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

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

Table of Contents

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

*Additional Merger Consideration*

In connection with the merger with JD Holdings, we agreed to pay to Mr. Dahan the following contingent consideration in the applicable fiscal year for 120 months following October 25, 2007:

- No contingent consideration if the gross profit is less than \$11,250,000 in the applicable fiscal year;
- 11.33% of the gross profit from \$11,251,000 to \$22,500,000;
- 3% of the gross profit from \$22,501,000 to \$31,500,000;
- 2% of the gross profit from \$31,501,000 to \$40,500,000; and
- 1% of the gross profit above \$40,501,000.

The additional merger consideration, or contingent consideration, was paid in advance on a monthly basis based upon estimates of gross profits after the assumption that the payments were likely to be paid. At the end of each quarter, any overpayments were offset against future payments and any significant underpayments were made.

Under the Financial Accounting Standards Board (FASB) Accounting Standards Codification, or ASC, accounting for consideration transferred to settle a contingency based on earnings or other performance measures, certain criteria is used to determine whether contingent consideration based on earnings or other performance measures should be accounted for as (1) adjustment of the purchase price of the acquired enterprise or (2) compensation for services, use of property or profit sharing. The determination of how to account for the contingent consideration is a matter of judgment that depends on the relevant facts and circumstances. The advanced contingent consideration payments are accounted for as operating expense.

On February 18, 2013, we entered into a new agreement with Mr. Dahan that provided certainty of payments to him by removing the contingencies related to the contingent consideration payments described above. This agreement fixed the overall amount to be paid by us for the remaining months of year six through year 10 with payments being made over an accelerated time period until November 2015 instead of October 2017. Under the agreement, the total aggregate amount Mr. Dahan will receive is \$9,168,000. We recorded a one-time charge as an expense for the full amount in the first quarter of fiscal 2013. In addition, Mr. Dahan agreed to a restrictive covenant relating to non-competition and non-solicitation until November 30, 2016 in addition to the restrictive covenant in the original merger agreement. Because we are in default under our term loan credit agreement and revolving credit agreement, we are currently prohibited from making buy-out payments to Mr. Dahan.

#### *Income Taxes*

As part of the process of preparing our consolidated financial statements, management is required to estimate income taxes in each of the jurisdictions in which we operate. The process involves estimating actual current tax expense along with assessing temporary differences resulting from differing treatment of items for book and tax purposes. These timing differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheet. Management records a valuation allowance to reduce its deferred tax assets to the amount that is more likely than not to be realized. Management has considered future taxable income and ongoing tax planning strategies in assessing the need for the valuation allowance. Increases in the valuation allowance result in additional expense to be reflected within the tax provision in the consolidated statement of income. Reserves are also estimated for ongoing audits regarding federal and state issues that are currently unresolved. We routinely monitor the potential impact of these situations.

Table of Contents

*Contingencies*

We record an estimated loss from a loss contingency when information available prior to issuance of our financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Accounting for contingencies such as legal and income tax matters requires management to use judgment. Many of these legal and tax contingencies can take years to be resolved. Generally, as the time period increases over which the uncertainties are resolved, the likelihood of changes to the estimate of the ultimate outcome increases. Management believes that the accruals for these matters are adequate. Should events or circumstances change, we could have to record additional accruals.

*Stock Based Compensation*

We account for stock-based compensation in accordance with the ASC standards. We elected the modified prospective method where prior periods are not revised for comparative purposes. Under the fair value recognition provisions, stock based compensation is measured at grant date based upon the fair value of the award and expense is recognized on a straight-line basis over the vesting period. We use the Black-Scholes option pricing model to determine the fair value of stock options, which requires management to use estimates and assumptions. The determination of the fair value of stock based option awards on the date of grant is based upon the exercise price as well as assumptions regarding subjective variables. These variables include our expected life of the option, expected stock price volatility over the term of the award, determination of a risk free interest rate and an estimated dividend yield. We estimate the expected life of the option by calculating the average term based upon historical experience. We estimate the expected stock price volatility by using implied volatility in market traded stock over the same period as the vesting period. We base the risk-free interest rate on zero coupon yields implied from United States Treasury issues with remaining terms similar to the term on the options. We do not expect to pay dividends in the foreseeable future and therefore use an expected dividend yield of zero. If factors change or we employ different assumptions for estimating fair value of the stock option, our estimates may be different than future estimates or actual values realized upon the exercise, expiration, early termination or forfeiture of those awards in the future. At this time, we believe that our current method for accounting for stock based compensation is reasonable. Furthermore, an entity may elect either an accelerated recognition method or a straight-line recognition method for awards subject to graded vesting based on a service condition, regardless of how the fair value of the award is measured. For all stock based compensation awards that contain graded vesting based on service conditions, we have elected to apply a straight-line recognition method to account for these awards. However, guidance is relatively new and the application of these principles over time may be subject to further interpretation or refinement. See Notes to Consolidated Financial Statements Note 2 Summary of Significant Accounting Policies Stock-Based Compensation and Notes to Consolidated Financial Statements Note 12 Stockholders Equity Stock Incentive Plans in our Annual Report for additional discussion.

*Recent Accounting Pronouncements*

In May 2014, the Financial Accounting Standards Board, or FASB, issued a comprehensive new revenue recognition standard which will supersede previous existing revenue recognition guidance. The standard creates a five-step model for revenue recognition that requires companies to exercise judgment when considering contract terms and relevant facts and circumstances. The five-step model includes (1) identifying the contract, (2) identifying the separate performance obligations in the contract, (3) determining the transaction price, (4) allocating the transaction price to the separate performance obligations and (5) recognizing revenue when each performance obligation has been satisfied. The standard also requires expanded disclosures surrounding revenue recognition. The standard is effective for fiscal periods beginning after December 15, 2016 and allows for either full retrospective or modified retrospective adoption. We are currently evaluating the impact of the adoption of this standard on our consolidated financial statements.

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

In May 2015, FASB issued ASU 2015-08, *Business Combinations (Topic 805): Pushdown Accounting - Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115*, or ASU 2015-08. The amendments in ASU 2015-08 amend various SEC paragraphs included in the FASB's Accounting Standards Codification to reflect the issuance of Staff Accounting Bulletin No. 115, or SAB 115. SAB 115 rescinds portions of the interpretive guidance included in the SEC's Staff Accounting Bulletins series and brings existing guidance into conformity with ASU No. 2014-17, *Business Combinations (Topic 805): Pushdown Accounting*, which provides an acquired entity with an option to apply pushdown accounting in its separate financial statements upon occurrence of an event in which an acquirer obtains control of the acquired entity. We have adopted the amendments in ASU 2015-08, effective May 8, 2015, as the amendments in the update are effective upon issuance. The adoption did not have an impact on our Condensed Financial Statements.

Table of Contents

In April 2015, the FASB issued Accounting Standards Update No. 2015-03, *Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, or ASU 2015-03. ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. For public entities, ASU 2015-03 is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Early adoption is permitted for financial statements that have not been previously issued. ASU 2015-03 is to be applied on a retrospective basis and represents a change in accounting principle. We believe the adoption of ASU 2015-03 will not have a material effect on our consolidated financial statements.

*Going Concern*

The accompanying financial statements have been prepared assuming that we will continue as a going concern. While management is evaluating all options to cure the defaults under our term loan and revolving credit agreements, including refinancing, extending the indebtedness and exploring alternatives for other sources of capital for ongoing cash needs, there can be no assurance that we will be able to secure a resolution or refinance or extend the indebtedness and, accordingly, our liquidity and ability to operate could be adversely affected. We have engaged Carl Marks Advisory Group to assist us as we explore all alternatives. We are currently in discussions with our creditors under both of the term loan credit agreement and revolving credit agreement regarding a resolution to the defaults, and our ability to continue as a going concern is dependent upon us resolving the outstanding indebtedness. Our financial statements do not include any adjustments relating to the recoverability and classification of recorded assets, or the amounts and classifications of liabilities that might be necessary should we be unable to continue as a going concern.

**Item 3. Quantitative and Qualitative Disclosure About Market Risk.**

*Foreign Currency Risk*

Foreign currency exposures arise from transactions, including firm commitments and anticipated contracts, denominated in a currency other than an entity's functional currency and from foreign-denominated revenues translated into U.S. dollars. Changes in currency exchange rates may affect the relative prices at which we and our foreign competitors sell products in the same market and collect receivables from such sales. We generally sell our products in U.S. dollars. However, we sell a limited amount of our products to certain countries in Euros. We currently do not hedge our exposure to changes in foreign currency exchange rates as the amount of products sold would not be significantly impacted by rate fluctuations. We cannot assure you that foreign currency fluctuations will not have a material adverse impact on our financial condition and results of operations in the future. Management believes the exposure to adverse changes in exchange rates are not sufficiently material to warrant a hedging program.

We also source most of our products outside of the United States. However, we generally purchase our products in U.S. dollars. The cost of these products may be affected by changes in the value of the relevant currencies; however, our exposure to currency exchange rates is limited as a result of such companies outside of the United States accepting payment in U.S. dollars.

*Credit Risk*

We are exposed to credit risk primarily on our accounts receivable. We provide credit to customers in the ordinary course of business and perform ongoing credit evaluations. We believe that our exposure to concentrations of credit risk with respect to trade receivables is largely mitigated by our customer base. We believe that our allowance for doubtful accounts is sufficient to cover customer credit risks as of May 31, 2015.

*Inflation*

Inflationary factors such as increases in the cost of our product and overhead costs may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial position or results of operations in recent periods, a high rate of inflation in the future may have an adverse effect on our ability to maintain current levels of gross margin and selling, general and administrative expenses as a percentage of net revenues if the selling prices of our products do not increase with these increased costs.

*Interest Rate Risk*

Our obligations under our revolving credit agreement and term loan agreement bear interest at floating rates. As a result, we are sensitive to changes in prevailing interest rates. We believe that a one percent increase or decrease in market interest rates that affect our financial instruments may have an impact on earnings or cash flow during the next fiscal year, depending on the outstanding principal balance subject to such interest rates.

Table of Contents

**Item 4. Controls and Procedures.**

*Evaluation of Disclosure Controls and Procedures*

As of May 31, 2015, the end of the period covered by this periodic report, our management carried out an evaluation, with the participation of our Interim Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15(b) and 15d-15(b) under the Exchange Act.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms. In addition, disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that the information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to management, including our principal executive and principal financial officers or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosures. Management recognizes that a control system, no matter how well conceived and operated, can provide only reasonable assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues within the company have been detected. Therefore, assessing the costs and benefits of such controls and procedures necessarily involves the exercise of judgment by management. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives.

As of the end of the period covered by this report, our Interim Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

*Changes in Internal Control Over Financial Reporting*

We made no change in our internal control over financial reporting during the second quarter of the fiscal year covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**Item 1. Legal Proceedings.**

We are a party to lawsuits and other contingencies in the ordinary course of our business. We do not believe that we are a party to any material pending legal proceedings or that it is probable that the outcome of any individual action would have an adverse effect in the aggregate on our



financial condition. We do not believe that it is likely that an adverse outcome of individually insignificant actions in the aggregate would be sufficient enough, in number or in magnitude, to have a material adverse effect in the aggregate on our financial condition.

**Item 1A. Risk Factors.**

In addition to the other information set forth in this Quarterly Report, you should carefully consider the factors discussed under **Risk Factors** in our Annual Report as filed with the SEC. These risks could materially and adversely affect our business, financial condition and results of operations. The risks described in our Annual Report are not the only risks we face. Our operations could also be affected by additional factors that are not presently known to us or by factors that we currently consider immaterial to our business.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

None.

**Item 3. Defaults upon Senior Securities.**

None.

Table of Contents

**Item 4. Mine Safety Disclosure.**

Not Applicable.

**Item 5. Other Information.**

(a) None.

(b) On July 6, 2015, in connection with the approval and adoption of Amended and Restated Bylaws, our board of directors adopted new procedures by which security holders may recommend nominees to our board of directors. The Amended and Restated Bylaws provide, among other things, that to bring any business before an annual meeting, a stockholder must give our Secretary written notice no later than the close of business on the 90th day and no earlier than the opening of business on the 120th day before the anniversary of the preceding annual stockholder's meeting; provided, however, that if the annual meeting is set more than 30 days earlier or more than 60 days later than such anniversary date, notice by the stockholder must be received no earlier than the opening of business on the 120th day before the meeting and no later than the later of the close of business on the 90th day before the meeting or the close of business on the 10th day following public disclosure of the date of the annual meeting. Notwithstanding the previous sentence, for purposes of determining whether a stockholder's notice shall have been received in a timely manner for the annual meeting of stockholders in 2015, to be timely, a stockholder's notice must have been received not later than the close of business on August 15, 2015, nor earlier than the opening of business on July 15, 2015. Any stockholder proposal will be deemed to have satisfied the advance notice requirements if the stockholder has notified us of their intention to present a proposal at an annual meeting in compliance with Rule 14a-8 of the Securities Exchange Act of 1934, as amended, and such stockholder's proposal has been included in our proxy statement.

All stockholder nominations, in addition to meeting the notice requirements above, must set forth (i) as to each person whom the stockholder proposes to nominate for election as a director (A) the name, age, business address and residence address of the person, (B) the principal occupation or employment of the person, (C) the class or series and number of shares of capital stock that are owned of record or are directly or indirectly owned beneficially by the person, (D) any derivative instrument directly or indirectly owned beneficially by such nominee and any other direct or indirect opportunity to profit or share in any profit derived from any increase or decrease in the value of shares and (E) any other information relating to the person that would be required to be disclosed in a proxy statement or other filings required to be made in connection with solicitations of proxies for election of directors pursuant to Section 14 of the Exchange Act and the rules and regulations promulgated thereunder. In addition to complying with all applicable rules and regulations related to securities laws, the stockholder giving notice must provide certain information related to himself or herself as set forth in the Amended and Restated Bylaws along with a written consent of each proposed nominee to being named as a nominee and to serve as a director if elected. The stockholder (or a qualified representative of the stockholder) must also appear at the meeting of stockholders to present the nomination, otherwise such nomination shall be disregarded, notwithstanding that proxies may have been received.

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If the Board or the chairman of the meeting of stockholders determines that any nomination was not made in accordance with the Amended and Restated Bylaws, then such nomination shall not be considered at the meeting.

Table of Contents**Item 6. Exhibits.**

Exhibits (listed according to the number assigned in the table in Item 601 of Regulation S-K):

<b>Exhibit No.</b>	<b>Description</b>	<b>Document if Incorporated by Reference</b>
3.2	Amended and Restated Bylaws of Joe's Jeans Inc., adopted as of July 6, 2015.	Exhibit 3.2 to the Current Report on Form 8-K filed on July 8, 2015
10.1	Forbearance and Amendment No. 3 to Revolving Credit Agreement, dated as of June 26, 2015, by and among Joe's Jeans Subsidiary, Inc. and Hudson Clothing, LLC, Joe's Jeans Inc., certain subsidiaries of Joe's Jeans Inc. party thereto, The CIT Group/Commercial Services, Inc., as administrative agent and collateral agent, and the lenders party thereto.	Exhibit 10.5 to the Current Report on Form 8-K filed on July 1, 2015
10.2	Forbearance Agreement, dated as of June 26, 2015, by and among Joe's Jeans Subsidiary, Inc. and Hudson Clothing, LLC, Joe's Jeans Inc., certain subsidiaries of Joe's Jeans Inc. party thereto, Garrison Loan Agency Services LLC, as administrative agent, and collateral agent, and the lenders party thereto.	Exhibit 10.6 to the Current Report on Form 8-K filed on July 1, 2015
10.3	Employment Agreement by and between Joe's Jeans Inc. and Hamish Sandhu dated July 2, 2015	Exhibit 10.1 to the Current Report on Form 8-K filed on July 8, 2015
10.4	Amendment No. 2 to Revolving Credit Agreement, dated as of April 23, 2015, by and among Joe's Jeans Subsidiary, Inc. and Hudson Clothing, LLC, Joe's Jeans Inc., certain subsidiaries of Joe's Jeans Inc. party thereto, and The CIT Group/Commercial Services, Inc., as administrative agent and collateral agent.	Exhibit 10.2 to the Current Report on Form 8-K filed on April 29, 2015.
31.1	Certification of the Interim Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as amended	Filed herewith
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as amended	Filed herewith
32	Certification of the Interim Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
101	The following materials from Joe's Jeans Inc.'s Quarterly Report on Form 10-Q for the quarter ended May 31, 2015, formatted in XBRL (eXtensible Business Reporting Language); (i) Condensed Consolidated Statements of Net (Loss) Income and Comprehensive (Loss) Income for the three and six months ended May 31, 2015 and 2014, (ii) Condensed Consolidated Balance Sheets at May 31, 2015 and November 30, 2014, (iii) Condensed Consolidated Statements of Cash Flows for the three and six months ended May 31, 2015 and 2014, (iv) Condensed Consolidated Statements Stockholders' Equity as of May 31, 2015 and 2014 and (v) Notes to the Unaudited Condensed Consolidated Financial Statements.	Filed herewith



Table of Contents

**SIGNATURES**

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

**JOE S JEANS INC.**

July 10, 2015

/s/ Samuel J. Furrow  
Samuel J. Furrow  
Interim Chief Executive Officer (Principal Executive Officer) and  
Chairman of the Board of Directors

July 10, 2015

/s/ Hamish Sandhu  
Hamish Sandhu  
Chief Financial Officer (Principal Financial Officer and  
Principal Accounting Officer)

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