

Destination Maternity Corp
Form 10-Q
June 11, 2015

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 2, 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 0-21196

Destination Maternity Corporation

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction

13-3045573
(IRS Employer

of incorporation or organization)
232 Strawbridge Drive

Identification No.)

Moorestown, New Jersey

08057

(Address of principal executive offices) (Zip code)

(856) 291-9700

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Registrant's telephone number, including area code

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 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 the 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 (Do not check if a smaller reporting company) Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, \$.01 par value — 13,857,554 shares outstanding as of June 4, 2015

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

(unaudited)

	May 2, 2015	January 31, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	\$1,978	\$1,349
Trade receivables, net	13,348	9,203
Inventories	80,956	75,759
Deferred income taxes	12,820	14,281
Prepaid expenses and other current assets	17,246	12,986
Total current assets	126,348	113,578
Property, plant and equipment, net of accumulated depreciation and amortization of \$81,689 and \$80,735	92,578	90,135
Other assets:		
Deferred financing costs, net of accumulated amortization of \$494 and \$445	494	543
Other intangible assets, net of accumulated amortization of \$613 and \$588	1,128	1,128
Deferred income taxes	14,440	13,704
Other non-current assets	790	972
Total other assets	16,852	16,347
Total assets	\$235,778	\$220,060
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Line of credit borrowings	\$18,700	\$—
Current portion of long-term debt	2,593	2,801
Accounts payable	26,717	26,482
Accrued expenses and other current liabilities	43,549	46,862
Total current liabilities	91,559	76,145
Long-term debt	11,484	12,199
Deferred rent and other non-current liabilities	26,141	25,714
Total liabilities	129,184	114,058
Commitments and contingencies (Note 12)		

Stockholders' equity:

Preferred stock, 1,656,381 shares authorized:

Series B junior participating preferred stock, \$.01 par value; 300,000 shares authorized, none outstanding

Common stock, \$.01 par value; 20,000,000 shares authorized, 13,859,038 and 13,807,124 shares issued and outstanding, respectively	—	—
Additional paid-in capital	139	138
Retained earnings	103,190	102,370
Accumulated other comprehensive loss	3,332	3,558
Total stockholders' equity	(67)	(64)
Total liabilities and stockholders' equity	106,594	106,002
	\$235,778	\$220,060

The accompanying notes are an integral part of these Consolidated Financial Statements.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share amounts)

(unaudited)

	Three Months Ended	
	May 2, 2015	May 3, 2014
Net sales	\$ 141,612	\$ 143,476
Cost of goods sold	70,209	65,455
Gross profit	71,403	78,021
Selling, general and administrative expenses	64,036	64,519
Store closing, asset impairment and asset disposal expenses	1,008	333
Other charges	1,808	531
Operating income	4,551	12,638
Interest expense, net	429	101
Income before income taxes	4,122	12,537
Income tax provision	1,587	4,827
Net income	\$ 2,535	\$ 7,710
Net income per share—Basic	\$ 0.19	\$ 0.57
Average shares outstanding—Basic	13,581	13,472
Net income per share—Diluted	\$ 0.19	\$ 0.57
Average shares outstanding—Diluted	13,624	13,575

The accompanying notes are an integral part of these Consolidated Financial Statements.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(unaudited)

	Three Months Ended	
	May 2, 2015	May 3, 2014
Net income	\$2,535	\$7,710
Foreign currency translation adjustments	(3)	6
Comprehensive income	\$2,532	\$7,716

The accompanying notes are an integral part of these Consolidated Financial Statements.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

(unaudited)

	Common Stock Number of Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance as of January 31, 2015	13,807	\$ 138	\$ 102,370	\$ 3,558	\$ (64)	\$ 106,002
Net income	—	—	—	2,535	—	2,535
Foreign currency translation adjustments	—	—	—	—	(3)	(3)
Cash dividends	—	—	—	(2,761)	—	(2,761)
Stock-based compensation	51	1	846	—	—	847
Exercise of stock options, net	4	—	37	—	—	37
Tax benefit shortfall from stock option exercises and restricted stock vesting	—	—	(12)	—	—	(12)
Repurchase and retirement of common stock	(3)	—	(51)	—	—	(51)
Balance as of May 2, 2015	13,859	\$ 139	\$ 103,190	\$ 3,332	\$ (67)	\$ 106,594
Balance as of February 1, 2014	13,712	\$ 137	\$ 99,527	\$ 24,574	\$ (66)	\$ 124,172
Net income	—	—	—	7,710	—	7,710
Foreign currency translation adjustments	—	—	—	—	6	6
Cash dividends	—	—	—	(2,735)	—	(2,735)
Stock-based compensation	(4)	—	1,065	—	—	1,065
Exercise of stock options, net	1	—	9	—	—	9
Excess tax benefit from stock option exercises and restricted stock vesting	—	—	99	—	—	99
Repurchase and retirement of common stock	(4)	—	(115)	—	—	(115)
Balance as of May 3, 2014	13,705	\$ 137	\$ 100,585	\$ 29,549	\$ (60)	\$ 130,211

The accompanying notes are an integral part of these Consolidated Financial Statements.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Three Months Ended	
	May 2, 2015	May 3, 2014
Operating Activities		
Net income	\$2,535	\$7,710
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,010	3,870
Stock-based compensation expense	847	1,065
Loss on impairment of long-lived assets	792	315
Loss (gain) on disposal of assets	154	(81)
Deferred income tax benefit (provision)	631	(746)
Amortization of deferred financing costs	49	50
Changes in assets and liabilities:		
Decrease (increase) in:		
Trade receivables	(4,145)	(5,693)
Inventories	(5,197)	(1,939)
Prepaid expenses and other current assets	(4,260)	(4,176)
Other non-current assets	182	(35)
Increase (decrease) in:		
Accounts payable, accrued expenses and other current liabilities	(2,990)	7,932
Deferred rent and other non-current liabilities	331	4,368
Net cash (used in) provided by operating activities	(7,061)	12,640
Investing Activities		
Capital expenditures	(12,909)	(10,335)
Proceeds from sale of property, plant and equipment	8	22
Additions to intangible assets	(44)	(202)
Net cash used in investing activities	(12,945)	(10,515)
Financing Activities		
Increase (decrease) in cash overdraft	5,637	(1,758)
Increase in line of credit borrowings	18,700	—
Repayment of long-term debt	(923)	—
Withholding taxes on stock-based compensation paid in connection with repurchase of common stock	(51)	(115)
Cash dividends paid	(2,761)	(2,735)
Proceeds from exercise of stock options	37	9
Excess tax benefit from exercise of stock options and restricted stock vesting	—	99
Net cash provided by (used in) financing activities	20,639	(4,500)
Effect of exchange rate changes on cash and cash equivalents	(4)	4

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Net Increase (Decrease) in Cash and Cash Equivalents	629	(2,371)
Cash and Cash Equivalents, Beginning of Period	1,349	17,574
Cash and Cash Equivalents, End of Period	\$1,978	\$15,203
Supplemental Disclosures of Cash Flow Information:		
Cash paid for interest	\$455	\$70
Cash paid for income taxes	\$56	\$1,196

The accompanying notes are an integral part of these Consolidated Financial Statements.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. BASIS OF FINANCIAL STATEMENT PRESENTATION

Destination Maternity Corporation and its subsidiaries (the “Company” or “Destination Maternity”) have historically operated on a fiscal year ending September 30 of each year. On December 4, 2014 the Company announced that its Board of Directors approved a change in its fiscal year end from September 30 to the Saturday nearest January 31 of each year. The fiscal year end change aligns the Company’s reporting cycle with the National Retail Federation (“NRF”) fiscal calendar. The change is effective with the Company’s fiscal year 2015, which began February 1, 2015 and will end January 30, 2016, and resulted in a four month transition period from October 1, 2014 to January 31, 2015. The accompanying unaudited consolidated financial statements for the three months ended May 2, 2015 and May 3, 2014 have been prepared in accordance with the requirements for Form 10-Q and Article 10 of Regulation S-X, and accordingly, certain information and footnote disclosures have been condensed or omitted. See the Company’s Annual Report on Form 10-K as of and for the year ended September 30, 2014 as filed with the Securities and Exchange Commission (“SEC”) for additional disclosures including a summary of the Company’s accounting policies.

In the opinion of management, the consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly the consolidated financial position, results of operations and cash flows of the Company for the periods presented. Since the Company’s operations are seasonal, the interim operating results of the Company may not be indicative of operating results for the full year.

References to fiscal years of the Company prior to fiscal 2015 refer to the fiscal years ended on September 30 in those years, unless otherwise indicated. For example, the Company’s “fiscal 2014” ended on September 30, 2014. The Company now operates on a fiscal year ending on the Saturday nearest January 31 of each year. References to the Company’s fiscal 2015 refer to the fiscal year, or periods within such fiscal year, which began February 1, 2015 and will end January 30, 2016.

2. EARNINGS PER SHARE (“EPS”) AND CASH DIVIDENDS

Basic net income (or earnings) per share (“Basic EPS”) is computed by dividing net income by the weighted average number of common shares outstanding, excluding restricted stock awards for which the restrictions have not lapsed. Diluted net income (or earnings) per share (“Diluted EPS”) is computed by dividing net income by the weighted average number of common shares outstanding, after giving effect to the potential dilution, if applicable, from the assumed exercise of outstanding stock options and from the assumed lapse of restrictions on restricted stock awards. Common shares issuable in connection with the award of performance-based restricted stock units (“RSUs”) are excluded from the calculation of EPS until the RSUs’ performance conditions are achieved and the shares in respect of the RSUs become issuable (see Note 10).

The following table summarizes the Basic EPS and Diluted EPS calculations (in thousands, except per share amounts):

Three Months Ended	
May 2, 2015	May 3, 2014

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	Net Income	Shares	EPS	Net Income	Shares	EPS
Basic EPS	\$2,535	13,581	\$0.19	\$7,710	13,472	\$0.57
Incremental shares from the assumed exercise of outstanding stock options	—	24		—	68	
Incremental shares from the assumed lapse of restrictions on restricted stock awards	—	19		—	35	
Diluted EPS	\$2,535	13,624	\$0.19	\$7,710	13,575	\$0.57

In addition to performance-based RSUs, for the three months ended May 2, 2015 and May 3, 2014 stock options and unvested restricted stock totaling 801,502 and 149,052 shares, respectively, were excluded from the calculation of Diluted EPS as their effect would have been antidilutive.

During the three months ended May 2, 2015 and May 3, 2014 the Company paid cash dividends totaling \$2,761,000 (or \$0.20 per share) and \$2,735,000 (or \$0.20 per share), respectively. On May 28, 2015 the Company declared a quarterly cash dividend of \$0.20 per share payable on July 23, 2015, which is projected to total approximately \$2,770,000.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

3. TRADE RECEIVABLES

Trade receivables are recorded based on revenue recognized for sales of the Company's merchandise and for other revenue earned by the Company through its marketing partnership programs and international franchise agreements, and are non-interest bearing. The Company evaluates the collectability of trade receivables based on a combination of factors, including aging of trade receivables, write-off experience, analysis of historical trends and expectations of future performance. An allowance for doubtful accounts is recorded for the amount of trade receivables that are considered unlikely to be collected. When the Company's collection efforts are unsuccessful, uncollectible trade receivables are charged against the allowance for doubtful accounts. As of May 2, 2015 and January 31, 2015 the Company's trade receivables were net of allowance for doubtful accounts of \$136,000 and \$132,000, respectively.

4. INVENTORIES

Inventories were comprised of the following (in thousands):

	May 2, 2015	January 31, 2015
Finished goods	\$76,594	\$ 69,455
Work-in-progress	1,320	2,414
Raw materials	3,042	3,890
	\$80,956	\$ 75,759

5. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities were comprised of the following (in thousands):

	May 2, 2015	January 31, 2015
Employee compensation and benefits	\$11,277	\$ 10,593
Insurance, primarily self-insurance reserves	6,218	5,888
Deferred rent	3,689	3,824
Gift certificates and store credits	3,688	4,704
Sales and use taxes	3,246	3,112
Accrued property, plant and equipment additions	2,457	3,619
Accounting and legal	2,124	1,998

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Product return reserve	2,099	2,084
Income taxes payable	—	129
Other	8,751	10,911
	\$43,549	\$46,862

6. LINE OF CREDIT AND LONG-TERM DEBT

On November 1, 2012 the Company entered into a five-year \$61,000,000 senior secured revolving credit facility (the “Credit Facility”), which replaced the Company’s former \$55,000,000 credit facility (the “Prior Credit Facility”). The Credit Facility consists of two tranches: 1) a senior secured revolving credit and letter of credit facility of up to \$55,000,000 (“Tranche A”) and 2) a senior secured first-in, last-out revolving credit facility of up to \$6,000,000 (“Tranche A-1”). The Credit Facility will mature on November 1, 2017. Upon the Company’s request and with the consent of the lender, permitted borrowings under Tranche A may be increased up to an additional \$15,000,000, in increments of \$2,500,000, up to a Tranche A maximum limit of \$70,000,000. In accordance with the terms of the Credit Facility, effective June 3, 2015 the Company’s permitted borrowings under Tranche A of the Credit Facility were increased by \$15,000,000 at the Company’s request. Proceeds from advances under the Credit Facility, with certain restrictions, were permitted to be used to repay then existing term loan or other debt, and may be used to provide financing for working capital, letters of credit, capital expenditures, dividends, share repurchases and other general corporate purposes. The Credit Facility contains various affirmative and negative covenants and representations and warranties. Under the Credit Facility, the Company is required to maintain minimum Excess Availability (as defined in the related Credit Facility agreement) equal to 10% of the Borrowing Base (as defined in the related Credit Facility agreement). The Credit Facility is secured by a security interest in the Company’s trade receivables,

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

inventory, letter of credit rights, cash, intangibles and certain other assets. The interest rate on outstanding borrowings is equal to, at the Company's election, either 1) the lender's base rate plus the applicable margin, or 2) a LIBOR rate plus the applicable margin. The applicable margin for base rate borrowings is 0.50% for Tranche A borrowings and 2.00% for Tranche A-1 borrowings. The applicable margin for LIBOR rate borrowings is 1.50% for Tranche A borrowings and 3.00% for Tranche A-1 borrowings. Tranche A-1 borrowings are deemed to be the first loans made and the last loans repaid. The Company also pays an unused line fee under the Credit Facility of 0.25% per annum. In connection with the execution of the Credit Facility, the Company incurred deferred financing costs of \$988,000.

As of May 2, 2015 the Company had \$18,700,000 outstanding borrowings under the Credit Facility, of which \$12,700,000 were Tranche A borrowings and \$6,000,000 were Tranche A-1 borrowings, and \$7,374,000 in letters of credit, with \$34,926,000 of availability under the Credit Facility. As of May 3, 2014 the Company had no outstanding borrowings under the Credit Facility and \$7,211,000 in letters of credit, with \$53,789,000 of availability under the Credit Facility. For the three months ended May 2, 2015 Tranche A borrowings had a weighted interest rate of 3.70% per annum, and Tranche A-1 borrowings had a weighted interest rate of 5.10% per annum. During the three months ended May 2, 2015 the Company's average level of direct borrowings was \$21,131,000, and the Company's maximum borrowings at any time were \$31,800,000. During the three months ended May 3, 2014 the Company did not have any direct borrowings under the Credit Facility.

During the four month transition period ended January 31, 2015 the Company received \$15,000,000 proceeds from a five-year equipment financing arrangement with its Credit Facility bank. The equipment note bears annual interest at 3.38%, with payments of \$272,000 (including interest) due monthly through December 2019. The equipment note is collateralized by substantially all of the material handling equipment currently being installed and tested at the Company's nearly completed distribution facility in Florence, New Jersey (see Note 8). As of May 2, 2015 there was \$14,077,000 outstanding under the equipment note.

7. FAIR VALUE MEASUREMENTS

The accounting standard for fair value measurements defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The standard establishes a framework for measuring fair value focused on exit price and creates a fair value hierarchy in order to increase the consistency and comparability of fair value measurements as follows:

Level 1 – Quoted market prices in active markets for identical assets or liabilities

Level 2 – Observable market-based inputs or inputs that are corroborated by observable market data

Level 3 – Unobservable inputs that are not corroborated by market data

At both May 2, 2015 and January 31, 2015 the Company had cash equivalents of \$4,000. The Company's cash equivalents consist of investments in money market funds for which the carrying value approximates fair value (based on Level 1 inputs) due to the short-term nature of those instruments. The carrying values of trade receivables and accounts payable approximate fair value due to the short-term nature of those instruments.

The Company's Credit Facility has variable interest rates that are tied to market indices. As of May 2, 2015 the Company had \$18,700,000 of direct borrowings outstanding under the Credit Facility. The carrying value of the Company's Credit Facility borrowings approximates fair value as the variable interest rates approximate current market rates, which the Company considers to be Level 2 inputs.

The Company's long-term debt bears interest at a fixed rate. The fair value of the Company's debt was determined using a discounted cash flow analysis based on interest rates currently available to the Company, which the Company considers to be Level 2 inputs. The difference between the carrying value and fair value of long-term debt held by the Company with a fixed rate of interest is not material.

8. OTHER CHARGES

In September 2013 the Company announced plans to relocate its corporate headquarters and distribution operations from Philadelphia, Pennsylvania to southern New Jersey. In January 2015 the Company completed the relocation of its corporate headquarters to Moorestown, New Jersey and expects to complete the relocation of its distribution operations to Florence, New Jersey

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

in mid-calendar 2015. In December 2014 the Company received notice of substantial completion and lease commencement from the landlord for the Florence distribution center building. Accordingly, the Florence lease, which has a 15-year term, commenced effective January 1, 2015, with the first rent payment due March 1, 2015. The Company is currently installing and testing its material handling equipment at the facility. During the three months ended May 2, 2015 and May 3, 2014 the Company incurred \$1,007,000 and \$531,000, respectively, of charges related to the closure of its existing facilities and the preparation for occupancy of its new facilities.

On August 11, 2014 the Company announced the appointment of Anthony M. Romano as the Company's new Chief Executive Officer ("CEO"). Subsequent to the CEO change, the Company commenced a program to evaluate its business processes, key management personnel and planning resources. In connection with this evaluation, the Company announced a change in its fiscal year (see below) and has started to implement changes to certain business processes, resulting in replacement of certain key management personnel and some reductions in headcount. The Company also implemented an improved product life cycle calendar and terminated an e-commerce development contract as it continues to improve its planning and allocation methodologies and e-commerce platform. During the three months ended May 2, 2015 the Company incurred \$801,000 of charges related to these management and organizational changes.

On December 4, 2014 the Company announced that its Board of Directors approved a change in its fiscal year end from September 30 to the Saturday nearest January 31 of each year. The fiscal year end change will align the Company's reporting cycle with the traditional 4-5-4 NRF calendar ending with January. The fiscal year change is expected to benefit the Company by providing a framework for more consistent product decisions, improved planning of marketing and promotional activities, and faster assimilation of new experienced retail hires.

A summary of the charges incurred in connection with the facilities relocations, management and organizational changes, and fiscal year change is as follows (in thousands):

	Three Months Ended	
	May 2, 2015	May 3, 2014
Facilities Relocations		
Pre-opening rent expense on new corporate headquarters and distribution facility	\$819	\$240
Accelerated depreciation and amortization expense	140	281
Other	48	10
Total facilities relocations	1,007	531
Management and Organizational Changes		
Consulting fees	711	—
Severance and related benefits	90	—

Total management and organizational changes	801	—
Total other charges	\$1,808	\$ 531

9. INCOME TAXES

As of May 2, 2015 the Company had \$1,572,000 of unrecognized tax benefits related to uncertain income tax positions, including accrued interest and penalties of \$516,000. The Company records interest and penalties related to unrecognized tax benefits in its income tax provision. If recognized, the portion of the liabilities for unrecognized tax benefits that would impact the Company's effective tax rate was \$988,000, net of federal benefit.

During the 12 months subsequent to May 2, 2015 it is reasonably possible that the gross unrecognized tax benefits could potentially decrease by \$524,000 (of which \$252,000 would affect the effective tax rate, net of federal benefit) for uncertain tax positions, including the continued effect of interest on unrecognized tax benefits and limitations on certain potential tax credits, offset by the effect of expiring statutes of limitations and settlements.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

The Company's United States Federal income tax returns for years ended September 30, 2011 and thereafter remain subject to examination by the United States Internal Revenue Service ("IRS"). The Company also files tax returns in Canada, India, Kuwait and numerous United States state jurisdictions, which have varying statutes of limitations. Generally, Canadian tax returns for tax years ended September 30, 2008 and thereafter, Indian tax returns for tax years ended March 31, 2010 and thereafter, Kuwaiti tax returns for tax years ended September 30, 2013 and thereafter, and United States state tax returns for tax years ended September 30, 2010 and thereafter, depending upon the jurisdiction, remain subject to examination. However, the statutes of limitations on certain of the Company's United States state tax returns remain open for years prior to fiscal 2010.

10. EQUITY AWARD PLANS

The Compensation Committee of the Company's Board of Directors established performance goals for the award of performance-based RSUs for four executive officers, under the Amended and Restated Destination Maternity Corporation 2005 Equity Incentive Plan, in each of April 2015 (the "Fiscal 2015 Awards"), December 2013 (the "Fiscal 2014 Awards") and November 2012 (the "Fiscal 2013 Awards"). The RSUs earned, if any, under the awards will be based on the Company's cumulative operating income, as defined in the applicable award agreement ("RSU Operating Income") for a specified three-year period ("Performance Period"). The grant of any RSUs under these awards will generally be further contingent on the continued employment of the executive officers with the Company through the dates on which the shares in respect of these RSUs, if any, are issued following the end of the applicable Performance Periods, as well as the achievement of certain minimum levels of RSU Operating Income in the final fiscal year of each applicable Performance Period. Any dividends declared on the shares of the Company's common stock underlying the RSUs will be credited as additional RSUs based on the fair market value of the Company's common stock on the dividend record date. The additional RSUs, if any, will be earned on the same terms as the original RSUs.

The following table sets forth the aggregate minimum, target and maximum RSUs, excluding RSUs from dividends declared, that may be earned by the executive officers for each fiscal year award cycle.

Awards	Performance Period	Minimum RSUs	Target RSUs	Maximum RSUs
Fiscal 2015 Awards	February 2, 2015 to January 28, 2017	23,253	46,504	69,757
Fiscal 2014 Awards	October 1, 2013 to September 30, 2016	15,113	30,224	45,337
Fiscal 2013 Awards	October 1, 2012 to September 30, 2015	18,541	37,080	55,621

During fiscal 2014, the Company determined that the Fiscal 2014 Awards and the Fiscal 2013 Awards were unlikely to be earned, even at the minimum level.

During the three months ended May 2, 2015 and May 3, 2014 certain stock option exercises and vesting restricted stock awards were net-share settled by the Company such that the Company withheld shares of the Company's common stock, which had a fair market value equivalent to the minimum statutory obligation for the applicable income and employment taxes for the awards, and the Company remitted the cash value to the appropriate taxing authorities. The total shares withheld, which were 3,090 and 4,073 shares, respectively, during the three months ended

May 2, 2015 and May 3, 2014, are reflected as repurchase of common stock in the accompanying financial statements, and were based on the value of the Company's common stock on the exercise or vesting date. The remaining shares, net of those withheld, were delivered to the award holders. Total payments for tax obligations to the tax authorities were \$51,000 and \$115,000 for the three months ended May 2, 2015 and May 3, 2014, respectively.

11. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014 the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606). ASU No. 2014-09 requires an entity to recognize revenue for the amount of consideration to which it expects to be entitled for the transfer of promised goods or services to customers. Additionally, ASU No. 2014-09 requires improved disclosures to help users of financial statements better understand the nature, amount, timing, and uncertainty of revenue that is recognized. The standard will replace most existing revenue recognition guidance in generally accepted accounting principles in the United States ("GAAP") when it becomes effective. ASU No. 2014-09 is effective for financial statements issued for annual reporting periods beginning after December 15, 2016 and interim periods within those years. Early adoption is not permitted. The impact from adoption of the new requirements of ASU No. 2014-09 on the Company's consolidated financial position or results of operations has not yet been determined.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

In April 2014 the FASB issued ASU No. 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. ASU No. 2014-08 changes the requirements for reporting discontinued operations and improves the definition of discontinued operations

by limiting discontinued operations reporting to disposals of components of an entity that represent strategic shifts that have (or will have) a major effect on an entity's operations and financial results. ASU No. 2014-08 also requires expanded disclosures for discontinued operations to provide users of financial statements with more information about the assets, liabilities, revenues, and expenses of discontinued operations. ASU No. 2014-08 is effective for all disposals (or classifications as held for sale) of components of an entity that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. Adoption of the new requirements of ASU No. 2014-08 is not expected to have a material impact on the Company's consolidated financial position or results of operations.

12. COMMITMENTS AND CONTINGENCIES

From time to time, the Company is named as a defendant in legal actions arising from normal business activities. Litigation is inherently unpredictable, and although the amount of any liability that could arise with respect to currently pending actions cannot be accurately predicted, the Company does not believe that the resolution of any pending action will have a material adverse effect on its financial position, results of operations or liquidity.

13. SEGMENT AND ENTERPRISE WIDE DISCLOSURES

Operating Segment. For purposes of the disclosure requirements for segments of a business enterprise, the Company has determined that its business is comprised of one operating segment: the design, manufacture and sale of maternity apparel and related accessories. While the Company offers a wide range of products for sale, the substantial portion of its products are initially distributed through the same distribution facilities, many of the Company's products are manufactured at common contract manufacturer production facilities, the Company's products are marketed through a common marketing department, and these products are sold to a similar customer base, consisting of expectant mothers.

Geographic Information. Geographic revenue information is allocated based on the country in which the products or services are sold, and in the case of international franchise revenues, on the location of the customer. Information concerning the Company's operations by geographic area was as follows (in thousands):

Three Months Ended

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May 2, May 3,
2015 2014

Net Sales to Unaffiliated Customers		
United States	\$132,924	\$137,158
Foreign	8,688	6,318

May 2, January
2015 31, 2015

Long-Lived Assets		
United States	\$90,430	\$88,120
Foreign	3,276	3,143

Major Customers. For the periods presented, the Company did not have any one customer who represented more than 10% of its net sales.

DESTINATION MATERNITY CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(unaudited)

14. INTEREST EXPENSE, NET

Interest expense, net was comprised of the following (in thousands):

	Three Months Ended	
	May	May
	2,	3,
	2015	2014
Interest expense	\$430	\$104
Interest income	(1)	(3)
Interest expense, net	\$429	\$101

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

We have historically operated on a fiscal year ending September 30 of each year. On December 4, 2014 we announced that our Board of Directors approved a change in our fiscal year end from September 30 to the Saturday nearest January 31 of each year. The fiscal year end change aligns our reporting cycle with the NRF fiscal calendar. The change is effective with our fiscal year 2015, which began February 1, 2015 and will end January 30, 2016, and resulted in a four month transition period from October 1, 2014 to January 31, 2015. References in this discussion to our fiscal years prior to fiscal 2015 refer to the fiscal years ended on September 30 in those years, unless otherwise indicated. For example, our "fiscal 2014" ended on September 30, 2014. References to our fiscal 2015 refer to the fiscal year, or periods within such fiscal year, which began February 1, 2015 and will end January 30, 2016. References to the transition period refer to the four month period from October 1, 2014 to January 31, 2015.

Overview

We are the leading designer and retailer of maternity apparel in the United States with 1,868 retail locations, including 557 stores in the United States, Puerto Rico and Canada, and 1,311 leased departments located within department stores and baby specialty stores throughout the United States and Puerto Rico. We are also the exclusive provider of maternity apparel to Kohl's®, which operates approximately 1,164 stores throughout the United States and offers maternity apparel in a significant number of its stores. We also sell merchandise on the Internet, primarily through DestinationMaternity.com and our various brand-specific websites. We have store franchise and product supply relationships in the Middle East, South Korea, Mexico and Israel. In November 2013 we announced our expansion into Mexico through a franchise agreement with the largest department store company in Mexico. In October 2014 we announced our expansion into Israel through a franchise agreement with one of Israel's largest and dominant fashion-retail chains. As of May 2, 2015 we have 128 international franchised locations, including 24 stand-alone stores operated under one of our retail nameplates and 104 shop-in-shop locations.

In assessing the performance of our business, we consider a variety of operational and financial measures. The key measures for determining how our business is performing are net income determined in accordance with GAAP ("net income") and the corresponding net income, or earnings per share (diluted), net income before certain charges or credits, when applicable, such as other charges, loss on extinguishment of debt, and certain infrequent income tax adjustments ("adjusted net income") and the corresponding earnings per share (diluted), Adjusted EBITDA (defined below), Adjusted EBITDA before other charges, net sales, comparable sales, and adjusted comparable sales. Adjusted EBITDA represents operating income before deduction for the following non-cash charges: 1) depreciation and amortization expense, 2) loss on impairment of tangible and intangible assets, 3) loss (gain) on disposal of assets, and 4) stock-based compensation expense.

Comparable sales figures represent sales at retail locations (which does not include licensed brand or international franchise relationships) that have been in operation by us for at least twelve full months at the beginning of the period for which such data is presented, as well as Internet sales. Comparable sales figures do not include retail locations opened during a period even if such location was opened in connection with the closure of other retail locations in the same geographic area (including, for example, the opening of a new Destination Maternity combo store or superstore). Also, our comparable sales figures generally do not include: 1) retail locations which change store nameplate, location type or format, 2) retail locations which are expanded, contracted or relocated if the square footage of the retail location has changed by 20% or more, or, if in the judgment of management, such expansion, contraction or relocation materially alters the comparability of the retail location (either with respect to the manner of its operation or otherwise), 3) in the case of relocations only, retail locations which are not in the same immediate geographical vicinity (such as, without limitation, the same mall, the same part of a mall, or the same street) after the relocation, or 4) retail locations which, in the judgment of management, have undergone other significant changes which materially alter the comparability of the retail location (either with respect to the manner of its operation or otherwise) (such as, for example only, in the case of closure of retail locations in connection with the cessation of a leased department

relationship where the manner of operation of such retail location has been materially altered prior to closure, or in the case of construction in, on or near a retail location, which significantly interferes with the customer traffic, visibility or operation of a retail location). There may be variations in the way in which other retailers calculate comparable sales. As a result, data in this quarterly report regarding our comparable sales may not be comparable to similar data made available by other retailers.

Following is a summary of our results for the first quarter of fiscal 2015 with regard to each of the key measures noted above:

First Quarter Fiscal 2015 Financial Results

Net income for the first quarter of fiscal 2015 was \$2.5 million, or \$0.19 per share (diluted), compared to net income of \$7.7 million, or \$0.57 per share (diluted), for the comparable three month period ended May 3, 2014.

Net income for the first quarter of fiscal 2015 includes other charges of 1) approximately \$0.6 million, net of tax, or \$0.05 per share (diluted), related to the relocations of our headquarters and distribution facilities and 2) \$0.5 million, net of tax, or \$0.04 per share (diluted), related to management and organizational changes. Net income for the three months ended May 3, 2014

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includes 1) other charges of \$0.3 million, net of tax, or approximately \$0.02 per share (diluted), related to the relocations of our headquarters and distribution facilities.

Adjusted net income for the first quarter of fiscal 2015 was \$3.7 million, or \$0.27 per share (diluted), compared to comparably adjusted net income for the three months ended May 3, 2014 of \$8.0 million, or \$0.59 per share (diluted). Adjusted EBITDA was \$10.4 million for the first quarter of fiscal 2015, compared to \$17.8 million of Adjusted EBITDA for the three months ended May 3, 2014.

Adjusted EBITDA before other charges was \$12.0 million for the first quarter of fiscal 2015, compared to \$18.1 million of Adjusted EBITDA before other charges for the three months ended May 3, 2014.

Net sales for the first quarter of fiscal 2015 decreased 1.3% to \$141.6 million from \$143.5 million for the three months ended May 3, 2014.

Comparable sales for the first quarter of fiscal 2015 decreased 1.1% compared to a comparable sales decrease of 4.0% for the three months ended May 3, 2014.

Results of Operations

The following table sets forth certain operating data as a percentage of net sales and as a percentage change for the three months ended May 2, 2015 and May 3, 2014:

	% of Net Sales (1) Three Months Ended		% Change Period to Period Favorable (Unfavorable) Three Months Ended	
	May 2, 2015	May 3, 2014	May 2, 2015 vs. May 3, 2014	
Net sales	100.0%	100.0%	(1.3)%
Cost of goods sold (2)	49.6	45.6	(7.3)
Gross profit	50.4	54.4	(8.5)
Selling, general and administrative expenses (3)	45.2	45.0	0.7	
Store closing, asset impairment and asset disposal expenses	0.7	0.2	(202.7)
Other charges	1.3	0.4	(240.5)
Operating income	3.2	8.8	(64.0)
Interest expense, net	0.3	0.1	(324.8)
Income before income taxes	2.9	8.7	(67.1)
Income tax (benefit) provision	1.1	3.4	67.1	
Net income	1.8	5.4	(67.1)%

(1) Components may not add to total due to rounding.

(2) "Cost of goods sold" includes merchandise costs (including customs duty expenses), expenses related to inventory shrinkage, product related corporate expenses (including expenses related to our payroll, benefit costs and operating expenses of our buying departments), inventory reserves (including lower of cost or market reserves), inbound freight charges, purchasing and receiving costs, inspection costs, warehousing costs, internal transfer costs, and the other costs of our distribution network.

(3) "Selling, general and administrative expenses" includes advertising and marketing expenses, corporate administrative expenses, store expenses (including store payroll and store occupancy expenses), and store opening expenses.

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The following tables set forth certain information concerning the number of our retail locations and international franchised locations for the periods indicated. Retail locations include stores and maternity apparel leased departments and exclude locations where Kohl's sells our products under an exclusive product and license agreement, and international franchised locations.

Retail Locations (1)	Three Months Ended		May 3, 2014	
	May 2, 2015		May 3, 2014	
	Leased Stores	Total Retail Locations	Leased Stores	Total Retail Locations