

CLAIRE'S STORES INC  
Form 10-Q  
September 14, 2018  
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**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 August 4, 2018**

**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 Nos. 1-8899, 333-148108 and 333-175171**

**Claire's Stores, Inc.**

**(Exact name of registrant as specified in its charter)**

**Florida**  
**(State or other jurisdiction of**  
**incorporation or organization)**

**59-0940416**  
**(I.R.S. Employer**  
**Identification No.)**

**2400 West Central Road,**  
**Hoffman Estates, Illinois**  
**(Address of principal executive offices)**  
**Registrant's telephone number, including area code: (847) 765-1100**

**60192**  
**(Zip 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

Explanatory Note: While registrant is not subject to the filing requirements of Section 13 or 15(d) of the Exchange Act, it has filed all reports pursuant to Section 13 or 15(d) of the Exchange Act during the preceding 12 months.

Indicate by check mark whether 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, smaller reporting company, or an emerging growth 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

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of September 1, 2018, 100 shares of the Registrant's common stock, \$0.001 par value, were outstanding.

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**CLAIRE S STORES, INC. AND SUBSIDIARIES**

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**Table of Contents****PART I. FINANCIAL INFORMATION****CLAIRE S STORES, INC. AND SUBSIDIARIES****(DEBTOR-IN-POSSESSION)****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

	August 4, 2018	February 3, 2018
	(In thousands, except share and per share amounts)	
ASSETS		
Current assets:		
Cash	\$ 69,445	\$ 42,446
Inventories	148,331	134,690
Prepaid expenses	36,889	32,284
Other current assets	21,737	26,858
Total current assets	276,402	236,278
Property and equipment:		
Furniture, fixtures and equipment	208,288	223,644
Leasehold improvements	279,104	301,338
	487,392	524,982
Accumulated depreciation and amortization	(387,631)	(405,284)
	99,761	119,698
Leased property under capital lease:		
Land and building	18,055	18,055
Accumulated depreciation and amortization	(7,667)	(7,216)
	10,388	10,839
Goodwill	1,132,575	1,132,575
Intangible assets, net of accumulated amortization of \$88,005 and \$87,295, respectively	450,145	457,078
Other assets	61,107	44,255
	1,643,827	1,633,908
Total assets	\$ 2,030,378	\$ 2,000,723
LIABILITIES AND STOCKHOLDER S DEFICIT		
Current liabilities:		
Current portion of long-term debt, net	\$ 84,732	\$ 1,894,039

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Debtor-in-possession term loan	60,000	
Trade accounts payable	55,272	62,965
Income taxes payable	14,096	4,049
Accrued interest payable	1,083	56,182
Accrued expenses and other current liabilities	101,216	94,934
<b>Total current liabilities</b>	<b>316,399</b>	<b>2,112,169</b>
Long-term debt, net	208,847	250,355
Obligation under capital lease	15,718	15,970
Deferred tax liability	29,179	32,614
Deferred rent expense	31,557	34,851
Unfavorable lease obligations and other long-term liabilities	8,646	10,040
	<b>293,947</b>	<b>343,830</b>
Liabilities subject to compromise	1,905,215	
Commitments and contingencies		
Stockholder's deficit:		
Common stock par value \$0.001 per share; authorized 1,000 shares; issued and outstanding 100 shares		
Additional paid-in capital	630,794	630,719
Accumulated other comprehensive loss, net of tax	(40,364)	(25,302)
Accumulated deficit	(1,075,613)	(1,060,693)
	<b>(485,183)</b>	<b>(455,276)</b>
<b>Total liabilities and stockholder's deficit</b>	<b>\$ 2,030,378</b>	<b>\$ 2,000,723</b>

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**Table of Contents****CLAIRE S STORES, INC. AND SUBSIDIARIES****(DEBTOR-IN-POSSESSION)****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND  
COMPREHENSIVE LOSS**

(in thousands)

	<b>Three Months Ended August 4, 2018</b>	<b>Three Months Ended July 29, 2017</b>	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Net sales	\$ 314,448	\$ 316,637	\$ 625,454	\$ 616,258
Cost of sales, occupancy and buying expenses (exclusive of depreciation and amortization shown separately below)	154,723	161,583	310,371	313,371
Gross profit	159,725	155,054	315,083	302,887
Other expenses (income):				
Selling, general and administrative	111,459	112,774	237,240	223,286
Depreciation and amortization	13,709	10,890	26,903	22,093
Severance and transaction-related costs	629	389	1,005	532
Other income, net	(3,348)	(2,171)	(7,354)	(4,872)
	122,449	121,882	257,794	241,039
Operating income before interest, reorganization items and income taxes	37,276	33,172	57,289	61,848
Reorganization items, net	30,453		40,462	
Interest expense, net	5,072	43,394	29,961	86,974
Income (loss) before income tax expense	1,751	(10,222)	(13,134)	(25,126)
Income tax expense	5,040	10,266	1,786	2,120
Net loss	\$ (3,289)	\$ (20,488)	\$ (14,920)	\$ (27,246)
Net loss	\$ (3,289)	\$ (20,488)	\$ (14,920)	\$ (27,246)
Other comprehensive (loss) income:				
Foreign currency translation adjustments	(1,067)	4,523	(3,602)	4,567
Net (loss) gain on intra-entity foreign currency transactions, net of tax (benefit) expense of \$(35), \$714, \$5 and \$944	(4,952)	7,593	(11,460)	9,474
Other comprehensive (loss) income	(6,019)	12,116	(15,062)	14,041

Comprehensive loss	\$	(9,308)	\$	(8,372)	\$	(29,982)	\$	(13,205)
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See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**Table of Contents****CLAIRE S STORES, INC. AND SUBSIDIARIES****(DEBTOR-IN-POSSESSION)****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Cash flows from operating activities:		
Net loss	\$ (14,920)	\$ (27,246)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	26,903	22,093
Reorganization items, net	40,462	
Amortization of lease rights and other assets	2,517	1,862
Amortization of debt issuance costs	1,613	4,312
Accretion of debt premium	(360)	(1,457)
Non-cash pay-in-kind interest expense	2,889	750
Net unfavorable accretion of lease obligations	9	(55)
Loss on sale/retirement of property and equipment, net	46	128
Stock-based compensation expense	75	156
(Increase) decrease in:		
Inventories	(17,945)	(22,083)
Prepaid expenses	(7,130)	(1,926)
Other assets	(6,461)	(75)
Increase (decrease) in:		
Trade accounts payable	(7,122)	(709)
Income taxes payable	12,249	(279)
Accrued interest payable	17,955	(155)
Accrued expenses and other liabilities	(6,128)	(6,994)
Deferred income taxes	(15,287)	(359)
Deferred rent expense	(2,460)	(1,196)
Net cash provided by (used in) operating activities	26,905	(33,233)
Cash flows from investing activities:		
Acquisition of property and equipment	(9,027)	(8,101)
Acquisition of intangible assets/lease rights	(100)	(38)
Net cash used in investing activities	(9,127)	(8,139)
Cash flows from financing activities:		
Proceeds from debtor-in-possession credit facility	57,000	



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Repayments under debtor-in-possession credit facility	(57,000)	
Proceeds from debtor-in-possession term loans	60,000	
Debt issuance costs related to debtor-in-possession financing	(4,470)	
Proceeds from revolving credit facilities	43,000	81,000
Payments on revolving credit facilities	(74,000)	(41,200)
Payment on current portion of long-term debt	(6,000)	(18,420)
Payments of unamortized interest related to long-term debt	(5,321)	(4,272)
Payment of debt issuance costs	(2)	(386)
Principal payments on capital lease	(200)	(156)
Net cash provided by financing activities	13,007	16,566
Effect of foreign currency exchange rate changes on cash and cash equivalents	(3,786)	203
Net increase (decrease) in cash and cash equivalents	26,999	(24,603)
Cash and cash equivalents, at beginning of period	42,446	55,792
Cash and cash equivalents, at end of period	\$ 69,445	\$ 31,189
Supplemental disclosure of cash flow information:		
Interest paid	\$ 13,002	\$ 87,454
Income taxes paid	2,112	3,927
Non-cash supplemental financing activities:		
Increase in term loans due 2021 from pay-in-kind interest	\$ 2,976	\$ 2,207
Decrease in adjustment to carrying value	2,976	2,207

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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**CLAIRE S STORES, INC. AND SUBSIDIARIES**

**(DEBTOR-IN-POSSESSION)**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Basis of Presentation**

The accompanying Unaudited Condensed Consolidated Financial Statements of Claire s Stores, Inc. (the Company ) have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair statement of the results for the interim periods presented have been included. These statements should be read in conjunction with the Consolidated Financial Statements and notes thereto included in the Annual Report on Form 10-K for the year ended February 3, 2018 filed with the Securities and Exchange Commission, including Note 2 to the Consolidated Financial Statements included therein, which discusses principles of consolidation and summary of significant accounting policies.

The Unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which require management to make certain estimates and assumptions about future events. These estimates and the underlying assumptions affect the amounts of assets and liabilities reported, disclosures regarding contingent assets and liabilities and reported amounts of revenues and expenses. Such estimates include, but are not limited to, the value of inventories, goodwill, intangible assets and other long-lived assets, legal contingencies and assumptions used in the calculation of income taxes, stock-based compensation, residual values and other items. These estimates and assumptions are based on management s best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. Management adjusts such estimates and assumptions when facts and circumstances dictate. Illiquid credit markets, volatile equity, foreign currency, and energy markets and declines in consumer spending have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates will be reflected in the financial statements in those future periods when the changes occur.

Due to the seasonal nature of the retail industry and the Company s business, the results of operations for interim periods of the year are not necessarily indicative of the results of operations for future quarters or on an annualized basis.

As discussed further in Note 2 entitled Bankruptcy Filing, on March 19, 2018 (the Commencement Date ), the Company and certain of its domestic subsidiaries (collectively with the Company, the Debtors ) commenced chapter 11 cases (the Chapter 11 Cases ) by filing voluntary petitions for reorganization under chapter 11 ( Chapter 11 ) of title 11 of the United States Code (the Bankruptcy Code ) with the United States Bankruptcy Court for the District of Delaware (the Bankruptcy Court ). The Debtors are authorized to continue to operate their businesses and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

**Ability to Continue as a Going Concern** - The accompanying Unaudited Condensed Consolidated Financial Statements have been prepared on a going concern basis of accounting, which contemplates continuity of operations, realization of assets, and satisfaction of liabilities and commitments in the normal course of business. The Company s

ability to continue as a going concern is contingent upon its ability to comply with the financial and other covenants contained in the debtor-in-possession credit facility (the "DIP Facility") described in Note 2. Bankruptcy Filing, the Bankruptcy Court's approval of its Chapter 11 plan of reorganization, and its ability to successfully implement a restructuring plan and obtain new financing, among other factors. The Company has significant indebtedness. The Company's

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level of indebtedness has adversely impacted and is continuing to adversely impact its financial condition. The Company's financial condition, the defaults under its debt agreements, and the risks and uncertainties surrounding the Chapter 11 Cases, raise substantial doubt as to the Company's ability to continue as a going concern.

As a result of the Chapter 11 Cases, the realization of assets and the satisfaction of liabilities are subject to uncertainty. The commencement of the Chapter 11 Cases constituted an event of default with respect to certain of the Company's existing debt obligations. While operating as debtors in possession under Chapter 11, the Company may sell or otherwise dispose of or liquidate assets or settle liabilities, subject to the approval of the Bankruptcy Court or as otherwise permitted in the ordinary course of business under the Bankruptcy Code and subject to restrictions contained in the DIP Credit Agreement (see Note 5 Debt) and applicable orders of the Bankruptcy Court, for amounts other than those reflected in the accompanying Unaudited Condensed Consolidated Financial Statements. Further, the Company's restructuring plan, to the extent confirmed by the Bankruptcy Court, could materially impact the amounts and classifications of assets and liabilities reported in its Unaudited Condensed Consolidated Financial Statements.

The Company plans to emerge from its Chapter 11 Cases after it obtains an order from the Bankruptcy Court confirming the Company's Proposed Plan (as defined below). Among other things, confirmation of the Proposed Plan will determine the rights and satisfy the claims of the Company's creditors and security holders in accordance with the terms of the Proposed Plan. A copy of the Debtors' Proposed Plan is available free of charge online at <https://cases.primeclerk.com/claiores/>.

## **2. Bankruptcy Filing**

### **Chapter 11 Proceedings**

On the Commencement Date, the Debtors commenced the Chapter 11 Cases by filing voluntary petitions for reorganization under Chapter 11 with the Bankruptcy Court. Pursuant to Rule 1015(b) of the Federal Rules of Bankruptcy Procedure, the Debtors' Chapter 11 Cases are being jointly administered for procedural purposes only under the caption *In re Claire's Stores, Inc., et al.*, Case No. 18-10584 (MFW). Documents filed on the docket of and other information related to the Chapter 11 Cases are available free of charge online at <https://cases.primeclerk.com/claiores/>.

In connection with the commencement of the Chapter 11 Cases, the Debtors entered into a Restructuring Support Agreement (the "Restructuring Support Agreement"), dated as of March 19, 2018, with Apollo Global Management, LLC, the Debtors' equity sponsor (the "Sponsor") and certain unaffiliated holders of first lien debt issued by the Company (each, an "Ad Hoc First Lien Holder" and, collectively, the "Ad Hoc First Lien Group" or the "Initial Consenting Holders"). On July 7, 2018, the Debtors and the Ad Hoc First Lien Group amended the Restructuring Support Agreement to permit the Debtors to solicit alternative proposals for (i) plans of reorganization or liquidation or (ii) the purchase of some or all of the Debtors' assets, and to modify certain milestones with respect to the Debtors' restructuring process.

Pursuant to the Restructuring Support Agreement, the Ad Hoc First Lien Group and Apollo agreed to support the pre-negotiated plan of reorganization that the Debtors seek to confirm. In accordance with the Restructuring Support Agreement, the Debtors filed the plan of reorganization (as amended, modified, or supplemented, the "Proposed Plan") and related disclosure statement (as amended, modified, or supplemented the "Disclosure Statement") with the Bankruptcy Court on April 12, 2018. The Debtors then amended the Proposed Plan on July 7, 2018 and again on July 16, 2018. On July 26, 2018, the Bankruptcy Court entered an order approving the Disclosure Statement, finding that the Disclosure Statement contained adequate information as required by the Bankruptcy Code. Additionally, the Bankruptcy Court approved solicitation and confirmation procedures for the Proposed Plan and scheduled a hearing

(the Confirmation Hearing ) for September 17, 2018 to consider confirmation of the Proposed Plan.

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### **Significant Bankruptcy Court Actions**

Following the Commencement Date, the Bankruptcy Court entered certain interim and final orders facilitating the Debtors' operational transition into Chapter 11. These orders authorized the Debtors to, among other things, pay certain pre-petition employee expenses and benefits, use their existing cash management system, maintain and administer customer programs, pay certain critical and foreign vendors, honor insurance-related obligations, and pay certain pre-petition taxes and related fees on a final basis. The Bankruptcy Court also approved the DIP Facility on a final basis.

### **Global Plan Settlement**

On July 15, 2018, the Debtors, the official committee of unsecured creditors appointed in the Chapter 11 Cases (the Creditors' Committee), the indenture trustee under the Company's Unsecured Notes (the Unsecured Notes Trustee), and the Ad Hoc First Lien Group entered into a settlement agreement (the Global Plan Settlement). Pursuant to the Global Plan Settlement, the Debtors resolved the formal and informal objections of the Creditors' Committee and the Unsecured Notes Trustee with respect to the Proposed Plan and the Debtors' restructuring, including with respect to (i) the enterprise value for the Debtors, together with their non-Debtor affiliates; (ii) value attributable to the Debtors' unencumbered assets; (iii) junior creditor recoveries; (iv) the treatment of intercompany claims and interests; (v) the releases and exculpations contemplated by the Proposed Plan, including with respect to the Sponsor and claims or causes of action arising from or related to the exchange transaction effectuated by the Company in 2016 (the 2016 Exchange); (vi) the terms of the new capital to be invested in the Company by the Ad Hoc First Lien Group; (vii) the allocation of assets and liabilities among the Debtors' Estates; and (viii) prospective lien challenges, claims, or causes of action that might be brought by or on behalf of the Debtors' Chapter 11 estates, including on account of the 2016 Exchange. The Bankruptcy Court will consider approval of the Global Plan Settlement at the Confirmation Hearing.

### **Settlement with FFI**

On August 31, 2018, the Debtors, FFI Fund Ltd., FYI Ltd. and their affiliates (collectively, the FFI Parties), holders of the Company's Unsecured Notes, and certain signatories to the Restructuring Support Agreement (the Requisite Consenting Creditors) entered into a Plan Support Agreement (the PSA), whereby the FFI Parties agreed to settle any and all potential objections they may have to the Proposed Plan and to support and vote all claims and interests held by the FFI Parties to accept the Proposed Plan and grant the releases provided for in the PSA. Pursuant to the PSA, the Debtors modified the Proposed Plan to increase the recoveries of holders of the Company's Unsecured Notes. The PSA became effective and binding on each of the Parties upon the execution and delivery of the PSA by each of (a) the Debtors, (b) the Requisite Consenting Creditors, and (c) the FFI Parties; provided that the PSA shall not be effective as to the Debtors until approved by the Bankruptcy Court upon confirmation of the Proposed Plan.

### **Oaktree's Standing Motion**

On July 19, 2018, Oaktree Capital Management, L.P. (Oaktree), the majority holder of the Company's Second Lien Notes, filed a motion in the Chapter 11 Cases seeking derivative standing to pursue certain avoidance actions with respect to the 2016 Exchange (the Standing Motion). The Debtors object to Oaktree's Standing Motion on the grounds that, among other things, Oaktree is prohibited from bringing such avoidance actions by virtue of its intercreditor obligations, Oaktree's Standing Motion is a premature objection to the approval of the Global Plan Settlement, and Oaktree cannot assert colorable claims with respect to such avoidance actions. The Bankruptcy Court will hold a hearing on Oaktree's Standing Motion on September 17, 2018.



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### **Executory Contracts**

Subject to certain exceptions, under the Bankruptcy Code, the Debtors may assume, assign, or reject certain executory contracts and unexpired leases subject to the approval of the Bankruptcy Court and certain other conditions. Generally, the rejection of an executory contract or unexpired lease is treated as a pre-petition breach of such executory contract or unexpired lease and, subject to certain exceptions, relieves the Debtors from performing their future obligations under such executory contract or unexpired lease but entitles the contract counterparty or lessor to a pre-petition general unsecured claim for damages caused by such deemed breach.

The Debtors have filed motions and received Bankruptcy Court approval for the rejection of 140 leases. As of August 4, 2018, the Debtors have rejected 83 leases. On August 24, 2018, the Debtors filed with the Bankruptcy Court a Rejected Executory Contracts and Unexpired Leases Schedule and Assumed Executory Contracts and Unexpired Leases Schedule with respect to those executory contracts and unexpired leases that either will be assumed or rejected pursuant to the Proposed Plan. Copies of these schedules are available free of charge online at <https://cases.primeclerk.com/claiores/>.

### **Key Employee Incentive and Retention Programs**

On May 5, 2018, the Debtors filed with the Bankruptcy Court a motion (the "KEIP/KERP Motion") seeking authority to implement a key employee incentive plan (the "KEIP") and a key employee retention program (the "KERP"). The KEIP provides performance metrics for senior members of the Debtors' management team to achieve in furtherance of the Debtors' business goals and, upon the achievement of those performance metrics, provides for maximum payments of up to approximately \$1.5 million in the aggregate per quarter through the end of the fourth quarter of Fiscal 2018. The KERP identifies valuable, hard-to-replace non-senior members of the Debtors' management team that play important roles in the Debtors' restructuring efforts, each performing crucial tasks to ensure a seamless transition into and an efficient emergence from Chapter 11. The KERP provides for payments of up to approximately \$1.5 million in the aggregate. The KERP participants would receive awards on the earlier of thirty days following the effective date of a Chapter 11 plan of reorganization and December 31, 2018, with the payment of such awards conditioned on the KERP participants' continued employment with the Company. The KEIP/KERP Motion was approved by the Bankruptcy Court on June 13, 2018.

### **Debtor-In-Possession Facility**

See Note 5 Debt for further discussion of the DIP Facility, which provides up to \$135.0 million in senior secured super-priority financing under a \$75.0 million DIP ABL Loan and a \$60.0 million DIP Term Loan.

### **Marketing Process**

On June 22, 2018, the Bankruptcy Court entered an order requiring the Debtors to solicit bids with respect to a sale or disposition by the Debtors of the Company's assets or an investment and/or sponsorship of a Chapter 11 plan of reorganization or liquidation. Additionally, the Bankruptcy Court established certain procedures (the "Bid Procedures") regarding the submission of certain bids (each, a "Qualified Bid" as defined in the Bid Procedures) with respect to some, all, or substantially all of the Company's assets or an investment in, and/or sponsorship of, a Chapter 11 plan of reorganization or liquidation. The deadline for the submission of Qualified Bids was August 31, 2018. The Debtors, in consultation with the Creditors' Committee, have determined that the Debtors have not received any Qualified Bids.





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Effective on March 19, 2018, the Company began to apply ASC, No. 852, Reorganizations, which is applicable to companies under Chapter 11 bankruptcy protection. It requires the financial statements for periods subsequent to the Chapter 11 filing to distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Expenses, realized gains and losses, and provisions for losses that are directly associated with reorganization proceedings must be reported separately as reorganization items, net in the Unaudited Condensed Consolidated Statements of Operations. In addition, the balance sheet must distinguish debtor pre-petition liabilities subject to compromise ( LSTC ) from liabilities of non-Debtor entities, pre-petition liabilities that are not subject to compromise and from post-petition liabilities in the accompanying Unaudited Condensed Consolidated Balance Sheet. LSTC are pre-petition obligations that are not fully secured and have at least a possibility of not being repaid at the full claim amount. Where there is uncertainty about whether a secured claim will be paid or impaired pursuant to the Chapter 11 Cases, the Company has classified the entire amount of the claim as a LSTC.

**Liabilities Subject to Compromise**

As a result of the commencement of the Chapter 11 Cases, the payment of pre-petition liabilities is generally subject to compromise pursuant to a plan of reorganization. Generally, actions to enforce or otherwise effect payment of pre-Commencement Date liabilities are stayed. Although payment of pre-petition claims generally is not permitted, the Bankruptcy Court granted the Debtors authority to pay certain pre-petition claims in designated categories and subject to certain terms and conditions. This relief generally was designed to preserve the value of the Debtors business and assets. Among other things, the Bankruptcy Court authorized, but did not require, the Debtors to pay certain pre-petition claims relating to employee wages and benefits, taxes, and certain vendors.

Pre-petition liabilities that are subject to compromise are required to be reported at the amounts expected to be allowed by the Bankruptcy Court, even if they may be settled for different amounts. The amounts classified as LSTC may be subject to future adjustments depending on Bankruptcy Court actions, further developments with respect to disputed claims, determination of secured status of certain claims, the determination as to the value of any collateral securing claims, proof of claims or other events.

Liabilities Subject to Compromise as of August 4, 2018 included the following components (in thousands):

	<b>August 4, 2018</b>
Debt (1)	\$ 1,806,363
Accrued interest on debt subject to compromise	73,054
Accounts payable, accrued expense and other liabilities	25,798
Total liabilities subject to compromise	\$ 1,905,215

(1) See Note 5 Debt for details of pre-petition debt reported as liabilities subject to compromise.

**Reorganization Items, Net**

Reorganization items, net represent amounts incurred after the Commencement Date as a direct result of the Bankruptcy and are comprised of the following for the three and six months ended August 4, 2018 (in thousands):

	<b>Three Months Ended August 4, 2018</b>	<b>Six Months Ended August 4, 2018</b>
Professional fees	\$ 22,744	\$ 33,697
Rejection of leases and other	7,277	7,277
Debtor-in-possession financing costs	432	4,470
Write-off of pre-petition debt issuance costs, debt premium, and adjustment in carrying value		(4,982)
<b>Total reorganization items, net</b>	<b>\$ 30,453</b>	<b>\$ 40,462</b>

**Table of Contents****3. Recent Accounting Pronouncements**

In October 2016, the FASB issued ASU 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory*. The update eliminates the exception for an intra-entity transfer of an asset other than inventory, which aligns the recognition of income tax consequences for inter-entity transfers of assets other than inventory by requiring the recognition of current and deferred income taxes resulting from an intra-entity transfer of such an asset when the transfer occurs rather than when it is sold to an external party. The Company adopted ASU 2016-16 as of the first day of Fiscal 2018 and it did not have a material impact on the Company's consolidated financial position, results of operations, or cash flow.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)*. The amendments in this update address how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230, Statement of Cash Flows, and other Topics. The Company adopted ASU 2016-15 as of the first day of Fiscal 2018 and it did not have a material impact on the Company's cash flows.

In March 2016, the FASB issued ASU 2016-04, *Liabilities - Extinguishments of Liabilities (Subtopic 405-20), Recognition of Breakage for Certain Prepaid Stored-Value Products*. The new guidance addresses diversity in practice related to the derecognition of a prepaid stored-value product liability. ASU 2016-04 is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. The Company adopted ASU 2016-04 as of the first day of Fiscal 2018 in connection with ASU 2014-09 and it did not have a material impact on its consolidated financial position, results of operations, or cash flows.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for substantially all leases. Leases will be classified as either financing or operating, with classification affecting the pattern of expense recognition in the statement of income. The new standard is effective for years beginning after December 15, 2018, including interim periods within those years. In July 2018, the FASB issued ASU 2018-11 which provided additional transition methods. The Company is currently quantifying the amount of lease assets and lease liabilities that it will recognize on its balance sheet. The Company's review of the requirements of Topic 842 is ongoing, and believes that the impact on its balance sheet, while not currently calculated, will be significant.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In August 2015, FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which delays the effective date of ASU 2014-09 by one year. FASB also agreed to allow entities to choose to adopt the standard as of the original effective date. In March 2016, FASB issued ASU No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, which clarifies the implementation guidance on principal versus agent considerations. The guidance includes indicators to assist an entity in evaluating whether it controls the good or the service before it is transferred to the customer. The new revenue recognition standard was effective for public entities for annual reporting periods beginning after December 15, 2017, and interim periods therein, that is, the first quarter of 2018. The new standard also permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the modified retrospective method). The Company adopted ASU 2014-09 as of the first day of Fiscal 2018 using the modified retrospective method. There were no changes to the consolidated financial position, results of operations, or cash flows as a result of the adoption and the timing and amount of its revenue

recognition remained substantially unchanged under this new guidance. The Company has included additional disclosures in Note 11 Segment Information showing disaggregation by revenue channel.

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**Accounting policies as a result of recently adopted accounting pronouncements**

**Revenue Recognition** Net sales is comprised of company-operated store sales, and other sales, which includes sales from concession, e-commerce and franchise. The Company excludes sales taxes collected from customers from Net sales in its Consolidated Statements of Operations and Comprehensive Income (Loss). Net Sales is presented net of an allowance for estimated returns, which is based on historic experience. The estimated liability for sales returns is based on the historical return levels, which is included in Accrued expenses and other current liabilities.

Revenue is recognized when performance obligations are satisfied through the transfer of control of promised goods to the Company's customers. Control transfers once a customer has the ability to direct the use of, and obtain substantially all of the benefits from, the product. This includes the transfer of legal title, physical possession, the risks and rewards of ownership, and customer acceptance. Revenue from company-operated stores is recognized as the customer takes possession of the merchandise. Revenue from concessions is recognized as the customer takes possession of the merchandise. Revenue from e-commerce is recognized when merchandise is shipped to the customer. Revenue from franchisees is recognized when merchandise is shipped from the Company to the franchisee. The Company accounts for the merchandise it sells to third parties under franchising and licensing agreements within Net Sales and Cost of sales, occupancy and buying expenses in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss). The franchise fees the Company charges under the franchising agreements are reported in Other income, net in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss).

Shipping fees billed to customers are recorded as revenue, and shipping costs are recognized within cost of sales in the same period the related revenue is recognized.

Upon purchase of a gift card or gift certificate, a liability is established for the cash value. The liability is included in Accrued expenses and other current liabilities. Revenue from gift card and gift certificate sales is recognized at the time of redemption. Unredeemed gift card and gift certificate breakage income is recorded as a reduction of Selling, general and administrative expenses. The Company records breakage income when the probability of redemption, based upon historical redemption patterns, is remote as there is currently no basis for estimating breakage income.

**4. Fair Value Measurements**

ASC 820, *Fair Value Measurement Disclosures*, defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Disclosures of the fair value of certain financial instruments are required, whether or not recognized in the Unaudited Condensed Consolidated Balance Sheets. Fair value is defined 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 and in the principal or most advantageous market for that asset or liability. There is a three-level valuation hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs are inputs market participants would use in valuing the asset or liability and are developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company's assumptions about the factors market participants would use in valuing the asset or liability.

**Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis**

The Company does not have any assets (liabilities) measured at fair value on a recurring basis.



**Table of Contents****Non-Financial Assets Measured at Fair Value on a Non-Recurring Basis**

The Company's non-financial assets, which include goodwill, intangible assets, and long-lived tangible assets, are not adjusted to fair value on a recurring basis. Fair value measures of non-financial assets are primarily used in the impairment analysis of these assets. Any resulting asset impairment would require that the non-financial asset be recorded at its fair value. The Company reviews goodwill and indefinite-lived intangible assets for impairment annually, during the fourth quarter of each fiscal year, or as circumstances indicate the possibility of impairment. The Company monitors the carrying value of definite-lived intangible assets and long-lived tangible assets for impairment whenever events or changes in circumstances indicate its carrying amount may not be recoverable.

**Financial Instruments Not Measured at Fair Value**

The Company's financial instruments consist primarily of cash and cash equivalents, accounts receivable, short-term debt, current liabilities and long-term debt. Cash and cash equivalents, accounts receivable, short-term debt, and current liabilities approximate fair market value due to the relatively short maturity of these financial instruments.

The Company considers all investments with a maturity of three months or less when acquired to be cash equivalents. The Company's cash equivalent instruments are valued using quoted market prices and are primarily U.S. Treasury securities. The revolving credit facilities approximate fair value due to the variable component of the interest rate. Excluding unamortized debt issuance costs, the estimated fair value of the Company's long-term debt (including current portion) was approximately \$1.12 billion as of August 4, 2018, compared to a carrying value of \$2.10 billion at that date. Excluding unamortized debt issuance costs, the estimated fair value of the Company's long-term debt (including current portion) was approximately \$1.28 billion as of February 3, 2018, compared to a carrying value of \$2.12 billion at that date. For publicly-traded debt, the fair value (estimated market value) is based on quoted market prices in less active markets. For non-publicly traded debt, fair value is estimated based on quoted prices for similar instruments. If measured at fair value in the financial statements, long-term debt excluding term loans would be classified as Level 2 in the fair value hierarchy, while term loans would be classified as Level 3 in the fair value hierarchy.

**5. Debt**

Debt as of August 4, 2018 and February 3, 2018 included the following components (in thousands):

	<b>August 4, 2018</b>	<b>February 3, 2018</b>
Short-term borrowings:		
Debtor-in-possession facility	\$ 60,000	\$
Current portion of long-term debt:		
Claire's Gibraltar Intermediate secured term loan due 2019	\$ 51,500	\$ 51,500
Claire's Gibraltar unsecured term loan due 2019	34,000	
9.0% Senior secured first lien notes due 2019		1,125,000
8.875% Senior secured second lien notes due 2019		222,300
6.125% Senior secured first lien notes due 2020		210,000



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7.75% Senior notes due 2020		216,742
9.0% Claire's Stores term loan due 2021		31,804
U.S. asset based lending credit facility due 2019		31,000
Unamortized premium (1)		3,642
Adjustment to carrying value (1)		12,483
Unamortized debt issuance cost (1)	(768)	(10,432)
Total current portion of long-term debt, net (1)	\$ 84,732	\$ 1,894,039

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	August 4, 2018	February 3, 2018
Debt subject to compromise:		
9.0% Senior secured first lien notes due 2019	\$ 1,125,000	\$
8.875% Senior secured second lien notes due 2019	222,300	
6.125% Senior secured first lien notes due 2020	210,000	
7.75% Senior notes due 2020	216,742	
9.0% Claire's Stores term loan due 2021	32,321	
<b>Total debt subject to compromise</b>	<b>\$ 1,806,363</b>	<b>\$</b>
Long-term debt:		
Claire's Gibraltar unsecured term loan due 2019	\$	\$ 40,000
11.0% CLSIP term loan due 2021 (2)	107,926	103,356
9.0% Claire's Gibraltar term loans due 2021	48,477	47,701
Adjustment to carrying value	52,444	59,298
<b>Total long-term debt, net</b>	<b>\$ 208,847</b>	<b>\$ 250,355</b>
Obligation under capital lease (including current portion)	\$ 16,188	\$ 16,388

- (1) LSTC must be reported at the amounts expected to be allowed by the Bankruptcy Court. The carrying value of the debt will be adjusted as claims are approved. As of August 4, 2018, the Company wrote off \$5.0 million of debt issuance costs, debt premium, and the adjustment to carrying value to present the debt at the outstanding face value. The write-offs are included within reorganization items, net in the Unaudited Condensed Consolidated Statements of Operations. See Note 2 Bankruptcy Filing for additional details.

- (2) See CLSIP Forbearance Agreement below for discussion of increased interest rate.

**Debtor-In-Possession Facility**

On March 22, 2018, the Company, pursuant to a commitment letter dated as of March 11, 2018 and previously disclosed on the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on March 19, 2018, and in connection with the Chapter 11 Cases and as a debtor in possession pursuant to the Bankruptcy Code, entered into a Credit Agreement (the "DIP Credit Agreement") among the Company, Claire's Inc., a Delaware corporation ( "Parent"), certain of the Company's subsidiaries (as described below), the lenders from time to time party thereto (the "Lenders") and Citibank, N.A., as administrative agent and collateral agent for the Lenders (in such capacities, the "Administrative Agent"), pursuant to which, among other things, the Lenders have provided (i) a senior secured superpriority non-amortizing asset-based revolving facility in an aggregate principal amount of \$75,000,000 (the "DIP ABL Loan"), with up to \$10,000,000 of such DIP ABL Loan available for the issuance of standby letters of credit and (ii) a superpriority senior secured last-out term facility in an aggregate principal amount of \$60,000,000 (the "DIP Term Loan" and together with the DIP ABL Loan, the "DIP Facility"). The DIP Facility is guaranteed on a joint and several basis by Parent, and certain of the Company's subsidiaries, including BMS

Distributing Corp., a Delaware corporation, CBI Distributing Corp., a Delaware corporation, Claire's Boutiques, Inc., a Colorado corporation, Claire's Canada Corp., a Delaware corporation, Claire's Puerto Rico Corp., a Delaware corporation and CSI Canada LLC, a Delaware limited liability company.

The proceeds of the DIP ABL Loan extended on the DIP Closing Date were used to refinance all outstanding obligations and replace commitments under the ABL Credit Facility (described below), including cash collateralization of certain letters of credit previously issued, outstanding and undrawn as of March 22, 2018, the closing date of the DIP Facility (the "DIP Closing Date"), and to pay fees, costs and expenses incurred in connection with the DIP Facility. The proceeds of the DIP Facility will also be used for working capital and general corporate purposes and to fund certain fees payable to professional service providers in connection with the Chapter 11 Cases.

The DIP Facility will mature, subject to the satisfaction of certain conditions, on the earliest of (i) the one year anniversary of the DIP Closing Date, (ii) the effective date of a plan of reorganization, (iii) the date of closing of a sale of all or substantially all of the Company's assets pursuant to Section 363 of the Bankruptcy Code, (iv) the date on which acceleration of the outstanding loans, and the terminations of the commitments, occurs under the DIP Facility and (v) certain dates specified in connection with the Chapter 11 Cases and orders issued in connection therewith.

As of August 4, 2018, the Company had \$65.6 million of availability under the DIP ABL Loan, net of applicable reserves.

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### **Contractual interest on debt subject to compromise**

Effective as of the Commencement Date, the Company ceased recording interest expense on outstanding pre-petition debt subject to compromise. Contractual interest expense represents amounts due under the contractual terms of outstanding pre-petition debt classified as LSTC. For the quarter ended August 4, 2018, contractual interest expense of \$58.5 million related to LSTC has not been recorded in the financial statements.

### **ABL Credit Facility**

In March 2018, the Company paid an aggregate amount of \$71.0 million and, in addition, the related accrued interest associated with the extinguishment of the ABL Credit Facility.

### **CLSIP Forbearance Agreement**

CLSIP Holdings, CLSIP, Wilmington Trust, N.A., as Administrative Agent and Collateral Agent under the CLSIP Term Loan Agreement, and certain of the lenders constituting Required Lenders (as that term is defined by the CLSIP Term Loan Agreement) under the CLSIP Term Loan entered into a forbearance agreement dated as of April 19, 2018 (the CLSIP Forbearance ) providing that, among other things, such lenders will forbear from causing the CLSIP Term Loan to become immediately due and payable and from exercising remedies arising from such event of default or other events of default that may arise on account of the commencement of the Chapter 11 Cases and/or any other transaction and/or agreement contemplated by the Restructuring Support Agreement. The CLSIP Forbearance also increased the interest rate of the CLSIP Term Loan to bear 11.0% per annum. As a result of the CLSIP Forbearance, the CLSIP Term Loan is classified as long-term debt.

### **Debt Covenants**

The Company's debt agreements contain certain covenants that, among other things, subject to certain exceptions and other basket amounts, restrict its ability and the ability of its subsidiaries to:

incur additional indebtedness;

pay dividends or distributions on its capital stock, repurchase or retire its capital stock and redeem, repurchase or defease any subordinated indebtedness;

make certain investments;

create or incur certain liens;

create restrictions on the payment of dividends or other distributions to us from the Company's subsidiaries;

transfer or sell assets;

engage in certain transactions with its affiliates; and

merge or consolidate with other companies or transfer all or substantially all of its assets.

Certain of these covenants in the indentures governing the Company's note indebtedness, such as limitations on the Company's ability to make certain payments such as dividends, or incur debt, will no longer apply if the notes have investment grade ratings from both of the rating agencies of Moody's Investor Services, Inc. (Moody's) and Standard & Poor's Ratings Group (S&P) and no event of default has occurred. Since the date of issuance of the notes, the notes have not received investment grade ratings from Moody's or S&P. Accordingly, all of the covenants under the notes currently apply to the Company. None of the covenants under the notes, however, require the Company to maintain any particular financial ratio or other measure of financial performance.

See Note 4 Fair Value Measurements for related fair value disclosure on debt.

**Table of Contents****Europe Bank Credit Facilities**

The Company's non-U.S. subsidiaries have bank credit facilities totaling approximately \$1.9 million. The facilities are used for working capital requirements, letters of credit and various guarantees. These credit facilities have been arranged in accordance with customary lending practices in the respective country of operation. As of August 4, 2018, there was a reduction of \$1.7 million for outstanding bank guarantees, which reduces the borrowing availability to \$0.2 million as of that date.

**6. Commitments and Contingencies**

The Company is, from time to time, involved in litigation incidental to the conduct of its business, including personal injury litigation, litigation regarding merchandise sold, including product and safety concerns regarding heavy metal and chemical content in merchandise, litigation with respect to various employment matters, including litigation with present and former employees, wage and hour litigation and litigation regarding intellectual property rights.

The Company believes that current pending litigation will not have a material adverse effect on its consolidated financial position, results of operations or cash flows.

**7. Accumulated Other Comprehensive Loss**

The following summary sets forth the components of accumulated other comprehensive loss, net of tax as follows (in thousands, net of tax):

	<b>Total (1)</b>
Balance as of February 3, 2018	\$ (25,302)
Other comprehensive loss	(15,062)
Balance as of August 4, 2018	\$ (40,364)

(1) Represents foreign currency items and \$5.7 million of other income associated with expired derivative instruments.

**8. Stock Options and Stock-Based Compensation**

The following is a summary of activity in the Company's stock option plan for the six months ended August 4, 2018:

	<b>Number of Shares</b>	<b>Weighted- Average Exercise Price</b>	<b>Weighted- Average Remaining Contractual Term (Years)</b>
Outstanding as of February 3, 2018	3,224,326	\$ 5.18	
Options granted			

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Options exercised				
Options forfeited	(17,511)	\$	2.83	
Options expired	(154,887)	\$	9.48	
Outstanding as of August 4, 2018	3,051,928	\$	4.98	3.6
Options vested and expected to vest as of August 4, 2018	2,938,253	\$	5.10	3.5
Exercisable as of August 4, 2018	1,892,324	\$	6.09	3.1

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There were no options granted during the six months ended August 4, 2018. The weighted average grant date fair value of options granted during the six months ended July 29, 2017 was \$0.39.

Stock-based compensation benefit is recorded in Selling, general and administrative expenses in the accompanying Unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss.

## **9. Income Taxes**

The effective income tax rate was 287.8% and (13.6)% for the three and six months ended August 4, 2018. This effective income tax rate differed from the statutory federal income tax rate of 21.0% primarily due to foreign losses with no associated income tax benefit and changes in valuation allowances.

The effective income tax rate was (100.4)% and (8.4)% for the three and six months ended July 29, 2017. This effective income tax rate differed from the statutory federal income tax rate of 35.0% primarily due to foreign tax rate differentials as compared to the U.S. statutory rate, changes in the valuation allowance and the correction of an immaterial error in the three months ended July 29, 2017.

On December 22, 2017, the President of the United States signed into law the Tax Cuts and Jobs Act of 2017 (the Tax Act). The Tax Act instituted fundamental changes to the US tax system. Staff Accounting Bulletin No. 118 (SAB 118) was issued to address the application of US GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed in reasonable detail to complete the accounting for certain income tax effects of the Tax Act. In accordance with SAB 118, Management calculated their best estimate of the impact of the Tax Act in the 2017 year-end income tax provision in accordance with their understanding of the Tax Act and available guidance. Also pursuant to SAB 118, certain additional impacts of the Tax Act remain open during the measurement period to include other indirect correlative impacts of the Tax Act, the Company's position with regards to the one-time mandatory transition tax and the state tax impacts of the Tax Act. As of the close of the second quarter, the Company continues to analyze the Tax Act in its entirety and refine its calculations, which could potentially impact the measurement of recorded tax balances. Any subsequent adjustment to the tax balances resulting from the analysis of the Tax Act, will be recorded to income tax expense in the fiscal quarter of 2018 when the analysis is completed.

## **10. Related Party Transactions**

### *Indebtedness*

As of August 4, 2018 and February 3, 2018, Parent and affiliates held \$68.6 million and \$65.6 million of the Company's indebtedness and the Company had no accrued interest payable associated with the indebtedness. For the three and six months ended August 4, 2018 and July 29, 2017, the Company recognized no interest expense related to the indebtedness held by Parent and affiliates as a result of the 2016 debt exchange whereby all future interest to be paid through maturity date was recorded at the time of the exchange.

### *Management Services Agreement*

On June 6, 2017, the Company and Parent entered into an Amended and Restated Management Services Agreement (the Management Services Agreement) with Apollo Management VI, L.P. (Apollo), Cowen & Co., LLC, as successor to Tri-Artisan Capital Partners, LLC (TACP), (Cowen), and together with Apollo, the Managers) and TACP Investments Claire's LLC (TACPI). The Management Services Agreement supersedes, amends and entirely restates the Management Services Agreement, dated as of May 29, 2007 by and among the Company, Parent, Apollo, TACP



and TACPI ( the Original Agreement ). Under the Management Service Agreement, the Managers have agreed to provide to the Company certain investment banking, management, consulting and financial planning services on an ongoing basis. The Managers will receive no fee for these services, but will be reimbursed by the Company for their out-of-pocket expenses. In the prior Management Services Agreement, the Managers were paid a \$3.0 million fee annually. In addition, under the Management Services Agreement, the Managers have agreed to provide to the Company certain financial advisory and investment banking

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services from time-to-time in connection with major financial transactions that may be undertaken by the Company or its subsidiaries in exchange for normal and customary fees as agreed by the Managers (or their affiliates) and the Company and Parent, taking into consideration all relevant factors. Under the Management Services Agreement, the Company and Parent have also agreed to provide the Managers (and their affiliates) with customary indemnification. The Management Services Agreement will terminate upon the earliest to occur of May 29, 2025 or the occurrence of certain termination events specified therein. The Company has not made any payments on account of the Management Services Agreement since commencing the Chapter 11 Cases.

In addition, on June 6, 2017, the Company and Cowen entered into a letter agreement (the "Cowen Management Agreement") pursuant to which Cowen agreed to provide the Company with certain financial advisory and investment banking services on a month-to-month basis. In return for such services, the Company agreed to pay Cowen a monthly cash fee of \$32,000, payable at the beginning of each month, and in addition, to reimburse Cowen for all reasonable out-of-pocket expenses. The Company also agreed to provide Cowen (and its affiliates) with customary indemnification. Both Cowen and the Company had the right to terminate the Cowen Management Agreement at any time during its term on 30 days prior written notice. While in effect, the terms of the Cowen Management Agreement were to govern in the event of any conflict between the Cowen Management Agreement and the terms of the Management Services Agreement referred to above. On September 1, 2017, the Company elected to terminate the Cowen Management Agreement effective as of September 30, 2017.

**11. Segment Information**

The Company is organized based on the geographic markets in which it operates. Under this structure, the Company currently has two reportable segments: North America and Europe. The Company accounts for the goods it sells to third parties under franchising and licensing agreements within "Net sales" and "Cost of sales, occupancy and buying expenses" in the Company's Unaudited Condensed Consolidated Statements of Operations and Comprehensive (Loss) Income within its North America segment. The franchise fees the Company charges under the franchising agreements are reported in "Other income, net" in the accompanying Unaudited Condensed Consolidated Statements of Operations and Comprehensive (Loss) Income within its Europe segment. Substantially all of the interest expense on the Company's outstanding debt and all of Reorganization Items, net is recorded in the Company's North America segment.

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Net sales, depreciation and amortization and operating income for the three and six months ended August 4, 2018 and July 29, 2017 are as follows (in thousands):

	<b>Three Months</b>		<b>Six Months</b>	
	<b>Three Months Ended August 4, 2018</b>	<b>Ended July 29, 2017</b>	<b>Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
<b>Net sales:</b>				
North America	\$ 199,454	\$ 196,033	\$ 406,388	\$ 391,993
Europe	114,994	120,604	219,066	224,265
Total net sales	314,448	316,637	625,454	616,258
<b>Depreciation and amortization:</b>				
North America	9,623	7,028	18,276	14,130
Europe	4,086	3,862	8,627	7,963
Total depreciation and amortization	13,709	10,890	26,903	22,093
<b>Operating income for reportable segments:</b>				
North America	28,511	16,306	55,139	42,016
Europe	9,394	17,255	3,155	20,364
Total operating income for reportable segments	37,905	33,561	58,294	62,380
Severance and transaction-related costs	629	389	1,005	532
Consolidated operating income	37,276	33,172	57,289	61,848
Reorganization items, net	30,453		40,462	
Interest expense, net	5,072	43,394	29,961	86,974
Consolidated income (loss) before income tax expense	\$ 1,751	\$ (10,222)	\$ (13,134)	\$ (25,126)

Excluded from operating income for the North America segment are severance and transaction-related costs of approximately \$0.3 million and \$0.3 million for the three months ended August 4, 2018 and July 29, 2017, respectively, and \$0.4 million and \$0.3 million for the six months ended August 4, 2018 and July 29, 2017, respectively.

Excluded from operating income for the Europe segment are severance and transaction-related costs of approximately \$0.3 million and \$0.1 million for the three months ended August 4, 2018 and July 29, 2017, respectively and \$0.6 million and \$0.2 million for the six months ended August 4, 2018 and July 29, 2017, respectively.



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Net sales by channel type and by segment for the three and six months ended August 4, 2018 are as follows (in thousands):

	<b>Three Months Ended August 4, 2018</b>	<b>Six Months Ended August 4, 2018</b>
<b>North America:</b>		
Company-operated net sales	\$ 186,518	\$ 376,453
Other net sales	12,936	29,935
Total net sales	199,454	406,388
<b>Europe:</b>		
Company-operated net sales	108,419	205,089
Other net sales	6,575	13,977
Total net sales	114,994	219,066
<b>Consolidated:</b>		
Company-operated net sales	294,937	581,542
Other net sales	19,511	43,912
Total net sales	\$ 314,448	\$ 625,454

**Table of Contents****12. Condensed Combined Debtor-In-Possession Financial Information**

The financial statements below represent the unaudited condensed combined financial statements of the Debtors. As of and for the three and six months ended August 4, 2018, the results of the Company's subsidiaries that are not part of the Chapter 11 Cases, are not included in these condensed combined financial statements.

Intercompany transactions among the Debtors have been eliminated in the financial statements contained herein. Intercompany transactions among the Debtors and the subsidiaries that are not part of the Chapter 11 Cases have not been eliminated in the Debtors' financial statements.

**Debtors Unaudited Condensed Combined Balance Sheet****August 4, 2018****(in thousands)**

<b>ASSETS</b>	
Current assets:	
Cash	\$ 27,825
Inventories	88,422
Prepaid expenses	20,935
Other current assets	13,400
Total current assets	150,582
Property and equipment:	
Furniture, fixtures and equipment	128,307
Leasehold improvements	167,133
	295,440
Accumulated depreciation and amortization	(240,023)
	55,417
Leased property under capital lease:	
Land and building	18,055
Accumulated depreciation and amortization	(7,667)
	10,388
Investment in non-filing entities	409,863
Goodwill	987,517
Intangible assets, net	188,223
Other assets	14,169

	1,599,772
Total assets	\$ 1,816,159
<b>LIABILITIES AND STOCKHOLDER'S DEFICIT</b>	
Current liabilities:	
Debtor-in-possession term loan	\$ 60,000
Trade accounts payable	18,549
Income taxes payable	7,849
Accrued interest payable	140
Accrued expenses and other current liabilities	61,907
Total current liabilities	148,445
Intercompany payables	174,547
Obligation under capital lease	15,718
Deferred tax liability	24,795
Deferred rent expense	20,692
Other long-term liabilities	8,646
	244,398
Liabilities subject to compromise	1,905,215
Stockholder's deficit:	
Common stock	
Additional paid in capital	630,794
Accumulated other comprehensive loss, net of tax	(40,364)
Accumulated deficit	(1,072,329)
	(481,899)
Total liabilities and stockholder's deficit	\$ 1,816,159

**Table of Contents****Debtors Unaudited Condensed Combined Statement of Operations and Comprehensive Income****(in thousands)**

	<b>Three Months Ended August 4, 2018</b>	<b>Six Months Ended August 4, 2018</b>
Net sales	\$ 184,157	\$ 376,611
Cost of sales, occupancy and buying expenses (exclusive of depreciation and amortization shown separately below)	89,654	179,919
Gross profit	94,503	196,692
Other expenses:		
Selling, general and administrative	62,921	136,553
Depreciation and amortization	9,202	17,389
Severance and transaction-related costs	264	348
Other income	(4,351)	(10,764)
	68,036	143,526
Operating income	26,467	53,166
Reorganization items, net	30,453	40,462
Interest expense, net	1,940	21,472
Loss before income taxes	(5,926)	(8,768)
Income tax expense	2,945	7,872
Loss from continuing operations	(8,871)	(16,640)
Equity in earnings of subsidiaries	24,836	51,928
Equity in earnings of non-filing entities	5,977	5,004
Net income	21,942	40,292
Foreign currency translation adjustments	(1,207)	(4,168)
Net loss on intra-entity foreign currency transactions, net of tax	(5,214)	(12,522)
Other comprehensive loss	(6,421)	(16,690)
Comprehensive income	\$ 15,521	\$ 23,602



**Table of Contents****Debtors Unaudited Condensed Combined Statement of Cash Flows****Six Months Ended August 4, 2018****(in thousands)**

<b>Cash flows from operating activities:</b>	
Net income	\$ 40,292
<b>Adjustments to reconcile net income to net cash used in operating activities:</b>	
Equity in earnings of subsidiaries	(51,928)
Equity in earnings of non-filing entities	(5,004)
Depreciation and amortization	17,389
Reorganization items, net	40,462
Amortization of debt issuance costs	898
Accretion of debt premium	(360)
Net accretion of unfavorable lease obligations	7
Loss on sale/retirement of property and equipment, net	44
Stock-based compensation expense	70
<b>(Increase) decrease in:</b>	
Inventories	(11,953)
Prepaid expenses	(4,557)
Other assets	(6,947)
<b>Increase (decrease) in:</b>	
Trade accounts payable	(8,076)
Income taxes payable	7,340
Accrued interest payable	17,386
Accrued expenses and other liabilities	(5,802)
Deferred income taxes	(2,586)
Deferred rent expense	(2,142)
<b>Net cash provided by operating activities</b>	<b>24,533</b>
<b>Cash flows from investing activities:</b>	
Acquisition of property and equipment	(6,553)
Acquisition of intangible assets/lease rights	(20)
<b>Net cash used in investing activities</b>	<b>(6,573)</b>
<b>Cash flows from financing activities:</b>	
Proceeds from debtor-in-possession credit facility	57,000
Repayments under debtor-in-possession credit facility	(57,000)
Proceeds from debtor-in-possession term loans	60,000
Debt issuance costs related to debtor-in-possession financing	(4,470)
Proceeds from revolving credit facilities	43,000

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Payments on revolving credit facilities	(74,000)
Payments of unamortized interest related to long-term debt	(925)
Principal payments on capital lease	(200)
Intercompany activity, net	(18,680)
Net cash provided by financing activities	4,725
Effect of foreign currency exchange rate changes on cash and cash equivalents	(2,207)
Net increase in cash and cash equivalents	20,478
Cash and cash equivalents, at beginning of period	7,347
Cash and cash equivalents, at end of period	27,825

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**13. Supplemental Financial Information**

On March 4, 2011, Claire's Stores, Inc. (referred to in this Note 13 as the "Issuer"), issued the Second Lien Notes. On February 28, 2012, March 12, 2012 and September 20, 2012, the Issuer issued the 9.0% Senior Secured First Lien Notes. On March 15, 2013, the Issuer issued the 6.125% Senior Secured First Lien Notes and on May 14, 2013, the Issuer issued the Unsecured Notes. The Second Lien Notes are irrevocably and unconditionally guaranteed, jointly and severally, by all wholly-owned domestic current and future subsidiaries of Claire's Stores, Inc. that guarantee the Company's ABL Credit Facility and U.S. Credit Facility. The First Lien Notes are unconditionally guaranteed, jointly and severally, by all wholly-owned domestic current and future subsidiaries of Claire's Stores, Inc. (subject to certain exceptions, including CLSIP LLC and CLSIP Holdings LLC). As of August 4, 2018, Claire's Stores, Inc. owned 100% of its domestic subsidiaries that guarantee the Notes. All guarantors are collectively referred to as the "Guarantors." The Company's other subsidiaries, principally its international subsidiaries including its European, Canadian and Asian subsidiaries (the "Non-Guarantors"), are not guarantors of these Notes.

The tables in the following pages present the unaudited condensed consolidating financial information for the Issuer, the Guarantors and the Non-Guarantors, together with eliminations, as of and for the periods indicated. The consolidating financial information may not necessarily be indicative of the financial position, results of operations or cash flows had the Issuer, Guarantors and Non-Guarantors operated as independent entities.

**Table of Contents****Unaudited Condensed Consolidating Balance Sheet****August 4, 2018****(in thousands)**

	<b>Issuer</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>ASSETS</b>					
Current assets:					
Cash	\$ 23,551	\$ 10,774	\$ 35,120	\$	\$ 69,445
Inventories		88,422	59,909		148,331
Prepaid expenses	8,300	12,635	15,954		36,889
Other current assets	418	12,982	8,337		21,737
Total current assets	32,269	124,813	119,320		276,402
Property and equipment:					
Furniture, fixtures and equipment	3,239	125,068	79,981		208,288
Leasehold improvements	1,315	165,818	111,971		279,104
	4,554	290,886	191,952		487,392
Accumulated depreciation and amortization	(3,834)	(236,189)	(147,608)		(387,631)
	720	54,697	44,344		99,761
Leased property under capital lease:					
Land and building		18,055			18,055
Accumulated depreciation and amortization		(7,667)			(7,667)
		10,388			10,388
Intercompany receivables		368,135	105,026	(473,161)	
Investment in subsidiaries	1,729,045	(40,870)		(1,688,175)	
Goodwill		987,517	145,058		1,132,575
Intangible assets, net	188,100	149,657	197,022	(84,634)	450,145
Other assets	8,000	6,169	46,938		61,107
	1,925,145	1,470,608	494,044	(2,245,970)	1,643,827
Total assets	\$ 1,958,134	\$ 1,660,506	\$ 657,708	\$ (2,245,970)	\$ 2,030,378

**LIABILITIES AND  
STOCKHOLDER'S EQUITY  
(DEFICIT)**

## Current liabilities:

Current portion of long-term debt, net	\$		\$	84,732	\$	84,732
Debtor-in-possession term loan		60,000				60,000
Trade accounts payable		2,323	16,226	36,723		55,272
Income taxes payable			7,849	6,247		14,096
Accrued interest payable		140	395	548		1,083
Accrued expenses and other current liabilities		27,113	34,794	39,309		101,216
<b>Total current liabilities</b>		<b>89,576</b>	<b>59,264</b>	<b>167,559</b>		<b>316,399</b>

Intercompany payables		473,161			(473,161)	
Long-term debt, net			143,810	65,037		208,847
Revolving credit facility, net						
Obligation under capital lease			15,718			15,718
Deferred tax liability			24,795	4,384		29,179
Deferred rent expense			20,692	10,865		31,557
Other long-term liabilities			8,646			8,646
		<b>473,161</b>	<b>213,661</b>	<b>80,286</b>	<b>(473,161)</b>	<b>293,947</b>

Liabilities subject to compromise		1,880,580	24,635			1,905,215
<b>Stockholder's equity (deficit):</b>						
Common stock			367	2	(369)	
Additional paid in capital		630,794	1,520,543	766,993	(2,287,536)	630,794
Accumulated other comprehensive income (loss),						
net of tax		(40,364)	(4,784)	(36,187)	40,971	(40,364)
<b>Accumulated deficit</b>		<b>(1,075,613)</b>	<b>(153,180)</b>	<b>(320,945)</b>	<b>474,125</b>	<b>(1,075,613)</b>
		<b>(485,183)</b>	<b>1,362,946</b>	<b>409,863</b>	<b>(1,772,809)</b>	<b>(485,183)</b>

<b>Total liabilities and stockholder's equity (deficit)</b>	<b>\$</b>	<b>1,958,134</b>	<b>\$</b>	<b>1,660,506</b>	<b>\$</b>	<b>657,708</b>	<b>\$</b>	<b>(2,245,970)</b>	<b>\$</b>	<b>2,030,378</b>
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**Table of Contents****Unaudited Condensed Consolidating Balance Sheet****February 3, 2018****(in thousands)**

	<b>Issuer</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ 4,203	\$ 9,644	\$ 28,599	\$	\$ 42,446
Inventories		76,469	58,221		134,690
Prepaid expenses	2,638	13,740	15,906		32,284
Other current assets	1,281	13,111	12,466		26,858
Total current assets	8,122	112,964	115,192		236,278
Property and equipment:					
Furniture, fixtures and equipment	3,075	133,664	86,905		223,644
Leasehold improvements	1,315	177,520	122,503		301,338
	4,390	311,184	209,408		524,982
Accumulated depreciation and amortization	(3,640)	(245,778)	(155,866)		(405,284)
	750	65,406	53,542		119,698
Leased property under capital lease:					
Land and building		18,055			18,055
Accumulated depreciation and amortization		(7,216)			(7,216)
		<b>10,839</b>			<b>10,839</b>
Intercompany receivables		299,768	121,143	(420,911)	
Investment in subsidiaries	1,688,098	(42,369)		(1,645,729)	
Goodwill		987,517	145,058		1,132,575
Intangible assets, net	188,100	149,678	203,934	(84,634)	457,078
Other assets	1,140	3,647	39,468		44,255
	1,877,338	1,398,241	509,603	(2,151,274)	1,633,908
Total assets	\$ 1,886,210	\$ 1,587,450	\$ 678,337	\$ (2,151,274)	\$ 2,000,723

**LIABILITIES AND  
STOCKHOLDER'S EQUITY  
(DEFICIT)**

## Current liabilities:

Current portion of long-term debt, net	\$ 1,843,582	\$	\$ 50,457	\$	\$ 1,894,039
Trade accounts payable	3,231	21,090	38,644		62,965
Income taxes payable		484	3,565		4,049
Accrued interest payable	55,808		374		56,182
Accrued expenses and other current liabilities	17,954	34,494	42,486		94,934
Total current liabilities	1,920,575	56,068	135,526		2,112,169

Intercompany payables	420,911			(420,911)	
Long-term debt, net		143,929	106,426		250,355
Obligation under capital lease		15,970			15,970
Deferred tax liability		25,963	6,651		32,614
Deferred rent expense		22,834	12,017		34,851
Unfavorable lease obligations and other long-term liabilities		10,040			10,040
	420,911	218,736	125,094	(420,911)	343,830

## Stockholder's equity (deficit):

Common stock		367	2	(369)	
Additional paid in capital	630,719	1,520,543	766,993	(2,287,536)	630,719
Accumulated other comprehensive income (loss), net of tax	(25,302)	(3,156)	(23,326)	26,482	(25,302)
Accumulated deficit	(1,060,693)	(205,108)	(325,952)	531,060	(1,060,693)
	(455,276)	1,312,646	417,717	(1,730,363)	(455,276)

Total liabilities and stockholder's equity (deficit)	\$ 1,886,210	\$ 1,587,450	\$ 678,337	\$ (2,151,274)	\$ 2,000,723
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**Table of Contents****Unaudited Condensed Consolidating Statement of Operations and Comprehensive Loss****For The Three Months Ended August 4, 2018****(in thousands)**

	<b>Issuer</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Net sales	\$	\$ 184,157	\$ 130,291	\$	\$ 314,448
Cost of sales, occupancy and buying expenses (exclusive of depreciation and amortization shown separately below)	2,828	86,826	65,069		154,723
Gross profit (deficit)	(2,828)	97,331	65,222		159,725
Other expenses:					
Selling, general and administrative	5,536	57,385	48,538		111,459
Depreciation and amortization	96	9,106	4,507		13,709
Severance and transaction-related costs	209	55	365		629
Other (income) expense	(1,541)	(2,810)	1,003		(3,348)
	4,300	63,736	54,413		122,449
Operating income (loss)	(7,128)	33,595	10,809		37,276
Reorganization items, net	24,832	5,621			30,453
Interest expense, net	1,406	929	2,737		5,072
Income (loss) before income taxes	(33,366)	27,045	8,072		1,751
Income tax expense		2,945	2,095		5,040
Income (loss) from continuing operations	(33,366)	24,100	5,977		(3,289)
Equity in earnings (loss) of subsidiaries	30,077	736		(30,813)	
Net income (loss)	(3,289)	24,836	5,977	(30,813)	(3,289)
Foreign currency translation adjustments	(1,067)	(140)	(520)	660	(1,067)
Net gain (loss) on intra-entity foreign currency transactions, net of tax	(4,952)	(262)	(4,952)	5,214	(4,952)
Other comprehensive income (loss)	(6,019)	(402)	(5,472)	5,874	(6,019)
Comprehensive income (loss)	\$ (9,308)	\$ 24,434	\$ 505	\$ (24,939)	\$ (9,308)

**Unaudited Condensed Consolidating Statement of Operations and Comprehensive Loss**



## For The Three Months Ended July 29, 2017

(in thousands)

	Issuer	Guarantors	Non-Guarantors	Eliminations	Consolidated
Net sales	\$	\$ 180,868	\$ 135,769	\$	\$ 316,637
Cost of sales, occupancy and buying expenses (exclusive of depreciation and amortization shown separately below)	3,017	89,864	68,702		161,583
Gross (deficit) profit	(3,017)	91,004	67,067		155,054
Other expenses:					
Selling, general and administrative	5,967	58,717	48,090		112,774
Depreciation and amortization	181	6,379	4,330		10,890
Severance and transaction-related costs	234	16	139		389
Other income, net	(918)	(112)	(1,141)		(2,171)
	5,464	65,000	51,418		121,882
Operating (loss) income	(8,481)	26,004	15,649		33,172
Interest expense, net	40,071	535	2,788		43,394
(Loss) income before income taxes	(48,552)	25,469	12,861		(10,222)
Income tax expense		121	10,145		10,266
(Loss) income from continuing operations	(48,552)	25,348	2,716		(20,488)
Equity in earnings (loss) of subsidiaries	28,064	(2,203)		(25,861)	
Net (loss) income	(20,488)	23,145	2,716	(25,861)	(20,488)
Foreign currency translation adjustments	4,523	1,080	(196)	(884)	4,523
Net gain (loss) on intra-entity foreign currency transactions, net of tax	7,593	2,199	7,588	(9,787)	7,593
Other comprehensive income (loss)	12,116	3,279	7,392	(10,671)	12,116
Comprehensive (loss) income	\$ (8,372)	\$ 26,424	\$ 10,108	\$ (36,532)	\$ (8,372)

**Table of Contents****Unaudited Condensed Consolidating Statement of Operations and Comprehensive Loss****For The Six Months Ended August 4, 2018****(in thousands)**

	<b>Issuer</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Net sales	\$	\$ 376,611	\$ 248,843	\$	\$ 625,454
Cost of sales, occupancy and buying expenses (exclusive of depreciation and amortization shown separately below)	6,642	173,277	130,452		310,371
Gross profit (deficit)	(6,642)	203,334	118,391		315,083
Other expenses:					
Selling, general and administrative	20,936	115,617	100,687		237,240
Depreciation and amortization	194	17,195	9,514		26,903
Severance and transaction-related costs	209	139	657		1,005
Other (income) expense	(12,321)	1,557	3,410		(7,354)
	9,018	134,508	114,268		257,794
Operating income (loss)	(15,660)	68,826	4,123		57,289
Reorganization items, net	34,841	5,621			40,462
Interest expense, net	20,430	4,326	5,205		29,961
Income (loss) before income taxes	(70,931)	58,879	(1,082)		(13,134)
Income tax benefit		7,872	(6,086)		1,786
Income (loss) from continuing operations	(70,931)	51,007	5,004		(14,920)
Equity in earnings (loss) of subsidiaries	56,011	921		(56,932)	
Net income (loss)	(14,920)	51,928	5,004	(56,932)	(14,920)
Foreign currency translation adjustments	(3,602)	(566)	(1,404)	1,970	(3,602)
Net gain (loss) on intra-entity foreign currency transactions, net of tax	(11,460)	(1,062)	(11,457)	12,519	(11,460)
Other comprehensive income (loss)	(15,062)	(1,628)	(12,861)	14,489	(15,062)
Comprehensive income (loss)	\$ (29,982)	\$ 50,300	\$ (7,857)	\$ (42,443)	\$ (29,982)

**Unaudited Condensed Consolidating Statement of Operations and Comprehensive Loss**

## For The Six Months Ended July 29, 2017

(in thousands)

	Issuer	Guarantors	Non-Guarantors	Eliminations	Consolidated
Net sales	\$	\$ 362,938	\$ 253,320	\$	\$ 616,258
Cost of sales, occupancy and buying expenses (exclusive of depreciation and amortization shown separately below)	6,179	176,063	131,129		313,371
Gross profit (deficit)	(6,179)	186,875	122,191		302,887
Other expenses:					
Selling, general and administrative	11,720	116,002	95,564		223,286
Depreciation and amortization	372	12,705	9,016		22,093
Severance and transaction-related costs	234	73	225		532
Other income, net	(2,855)	(304)	(1,713)		(4,872)
	9,471	128,476	103,092		241,039
Operating income (loss)	(15,650)	58,399	19,099		61,848
Interest expense, net	80,341	1,061	5,572		86,974
Income (loss) before income taxes	(95,991)	57,338	13,527		(25,126)
Income tax expense (benefit)		(943)	3,063		2,120
Income (loss) from continuing operations	(95,991)	58,281	10,464		(27,246)
Equity in earnings (loss) of subsidiaries	68,745	(2,157)		(66,588)	
Net income (loss)	(27,246)	56,124	10,464	(66,588)	(27,246)
Foreign currency translation adjustments	4,567	668	1,641	(2,309)	4,567
Net gain (loss) on intra-entity foreign currency transactions, net of tax	9,474	1,343	9,471	(10,814)	9,474
Other comprehensive income (loss)	14,041	2,011	11,112	(13,123)	14,041
Comprehensive income (loss)	\$ (13,205)	\$ 58,135	\$ 21,576	\$ (79,711)	\$ (13,205)

**Table of Contents****Unaudited Condensed Consolidating Statement of Cash Flows****Six Months Ended August 4, 2018****(in thousands)**

	<b>Issuer</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Cash flows from operating activities:					
Net income (loss)	\$ (14,920)	\$ 51,928	\$ 5,004	\$ (56,932)	\$ (14,920)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:					
Loss (equity) in earnings of subsidiaries	(56,011)	(921)		56,932	
Depreciation and amortization	194	17,195	9,514		26,903
Reorganization items, net	34,841	5,621			40,462
Amortization of lease rights and other assets			2,517		2,517
Amortization of debt issuance costs	898		715		1,613
Accretion of debt premium	(360)				(360)
Non-cash pay-in-kind interest expense		2,889			2,889
Net accretion of unfavorable lease obligations		7	2		9
Loss on sale/retirement of property and equipment, net		44	2		46
Stock-based compensation expense	70		5		75
(Increase) decrease in:					
Inventories		(11,953)	(5,992)		(17,945)
Prepaid expenses	(5,662)	1,105	(2,573)		(7,130)
Other assets	(5,998)	(949)	486		(6,461)
Increase (decrease) in:					
Trade accounts payable	(19,578)	11,502	954		(7,122)
Income taxes payable		7,340	4,909		12,249
Accrued interest payable	17,386	395	174		17,955
Accrued expenses and other liabilities	(7,648)	1,846	(326)		(6,128)
Deferred income taxes		(2,586)	(12,701)		(15,287)
Deferred rent expense		(2,142)	(318)		(2,460)
Net cash provided by (used in) operating activities	(56,788)	81,321	2,372		26,905
Cash flows from investing activities:					
Acquisition of property and equipment	(164)	(6,389)	(2,474)		(9,027)
Acquisition of intangible assets/lease rights		(20)	(80)		(100)

Net cash used in investing activities	(164)	(6,409)	(2,544)	(9,127)
Cash flows from financing activities:				
Proceeds from debtor-in-possession credit facility	57,000			57,000
Repayments under debtor-in-possession credit facility	(57,000)			(57,000)
Proceeds from debtor-in-possession term loans	60,000			60,000
Debt issuance costs related to debtor-in-possession financing	(4,470)			(4,470)
Proceeds from revolving credit facilities	43,000			43,000
Payments on revolving credit facilities	(74,000)			(74,000)
Payment on current portion of long-term debt			(6,000)	(6,000)
Payments of unamortized interest related to long-term debt	(925)	(3,008)	(1,388)	(5,321)
Payment of debt issuance costs			(2)	(2)
Principal payments on capital lease		(200)		(200)
Intercompany activity, net	52,695	(68,367)	15,672	
Net cash provided by (used in) financing activities	76,300	(71,575)	8,282	13,007
Effect of foreign currency exchange rate changes on cash and cash equivalents		(2,207)	(1,579)	(3,786)
Net increase (decrease) in cash and cash equivalents	19,348	1,130	6,521	26,999
Cash and cash equivalents, at beginning of period	4,203	9,644	28,599	42,446
Cash and cash equivalents, at end of period	23,551	10,774	35,120	69,445

**Table of Contents****Unaudited Condensed Consolidating Statement of Cash Flows****Six Months Ended July 29, 2017****(in thousands)**

	<b>Issuer</b>	<b>Guarantors</b>	<b>Non-Guarantors</b>	<b>Eliminations</b>	<b>Consolidated</b>
Cash flows from operating activities:					
Net income (loss)	\$ (27,246)	\$ 56,124	\$ 10,464	\$ (66,588)	\$ (27,246)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:					
Loss (equity) in earnings of subsidiaries	(68,745)	2,157		66,588	
Depreciation and amortization	372	12,705	9,016		22,093
Amortization of lease rights and other assets			1,862		1,862
Amortization of debt issuance costs	3,781		531		4,312
Accretion of debt premium	(1,457)				(1,457)
Non-cash pay-in-kind interest expense			750		750
Net accretion of unfavorable lease obligations		(56)	1		(55)
Loss on sale/retirement of property and equipment, net		126	2		128
Stock-based compensation expense	139		17		156
(Increase) decrease in:					
Inventories		(12,077)	(10,006)		(22,083)
Prepaid expenses	(675)	(84)	(1,167)		(1,926)
Other assets	(268)	(23)	216		(75)
Increase (decrease) in:					
Trade accounts payable	(912)	2,811	(2,608)		(709)
Income taxes payable		(967)	688		(279)
Accrued interest payable	73		(228)		(155)
Accrued expenses and other liabilities	(2,683)	(365)	(3,946)		(6,994)
Deferred income taxes			(359)		(359)
Deferred rent expense		(712)	(484)		(1,196)
Net cash provided by (used in) operating activities	(97,621)	59,639	4,749		(33,233)
Cash flows from investing activities:					
Acquisition of property and equipment		(5,111)	(2,990)		(8,101)
Acquisition of intangible assets/lease rights		(38)			(38)

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Net cash used in investing activities		(5,149)	(2,990)	(8,139)
<b>Cash flows from financing activities:</b>				
Proceeds from revolving credit facilities	81,000			81,000
Payments on revolving credit facilities	(41,200)			(41,200)
Payment on current portion of long-term debt	(18,420)			(18,420)
Payments of unamortized interest related to long-term debt	(743)	(2,415)	(1,114)	(4,272)
Payment of debt issuance costs			(386)	(386)
Principal payments on capital lease		(156)		(156)
Intercompany activity, net	79,605	(53,034)	(26,571)	
Net cash provided by (used in) financing activities	100,242	(55,605)	(28,071)	16,566
Effect of foreign currency exchange rate changes on cash and cash equivalents		2,928	(2,725)	203
Net increase (decrease) in cash and cash equivalents	2,621	1,813	(29,037)	(24,603)
Cash and cash equivalents, at beginning of period	3,038	3,005	49,749	55,792
Cash and cash equivalents, at end of period	\$ 5,659	\$ 4,818	\$ 20,712	\$ 31,189

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

Management's Discussion and Analysis of Financial Condition and Results of Operations is designed to provide the reader of the financial statements with a narrative on our results of operations, financial position and liquidity, risk management activities, and significant accounting policies and critical estimates. Management's Discussion and Analysis should be read in conjunction with the Unaudited Condensed Consolidated Financial Statements and related notes thereto contained elsewhere in this document.

We include a store in the calculation of same store sales once it has been in operation sixty weeks after its initial opening and we include sales from e-commerce. A store which is temporarily closed, such as for remodeling, is removed from the same store sales computation if it is closed for one week or more. The removal is effective prospectively upon the completion of the first fiscal week of closure. A store which is closed permanently, such as upon termination of the lease, is immediately removed from the same store sales computation. We compute same store sales on a local currency basis, which eliminates any impact for changes in foreign currency rates. Our calculation of same store sales may not be comparable to other retailers.

### **Voluntary Reorganization under Chapter 11**

On March 19, 2018 (the "Commencement Date"), the Company and certain of its domestic subsidiaries (collectively with the Company, the "Debtors"), commenced chapter 11 cases (the "Chapter 11 Cases") by filing voluntary petitions for reorganization under chapter 11 ("Chapter 11") of title 11 of the United States Code (the "Bankruptcy Code") with the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court"). The Debtors are authorized to continue to operate their businesses and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. Pursuant to Rule 1015(b) of the Federal Rules of Bankruptcy Procedure, the Debtors' Chapter 11 Cases are being jointly administered for procedural purposes only under the caption *In re Claire's Stores, Inc., et al.*, Case No. 18-10584 (MFW). Documents filed on the docket of and other information related to the Chapter 11 Cases are available free of charge online at <https://cases.primeclerk.com/claiores/>.

We are currently operating our business as debtors in possession in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court. After we commenced the Chapter 11 Cases, the Bankruptcy Court granted certain relief requested by the Debtors enabling us to conduct our business activities in the ordinary course, including, among other things and subject to the terms and conditions of such orders, authorizing us to pay employee wages and benefits, pay taxes and certain governmental fees and charges, continue to operate our cash management system in the ordinary course, and pay the pre-petition claims of certain of our vendors. For goods and services provided following the Commencement Date, we intend to pay vendors in full under normal terms.

Subject to certain exceptions, under the Bankruptcy Code, the commencement of the Chapter 11 Cases automatically enjoined, or stayed, the continuation of most judicial or administrative proceedings or filing of other actions against the Debtors or their property to recover, collect or secure a claim arising prior to the Commencement Date. Accordingly, although the filing of the commencement of the Chapter 11 Cases triggered defaults under the Debtors' funded debt obligations, creditors are stayed from taking any actions against the Debtors as a result of such defaults, subject to certain limited exceptions permitted by the Bankruptcy Code. Absent an order of the Bankruptcy Court, substantially all of the Debtors' pre-petition liabilities are subject to settlement under the Bankruptcy Code.

For the duration of the Debtors' Chapter 11 Cases, the Company's operations and ability to develop and execute its business plan are subject to the risks and uncertainties associated with the Chapter 11 process. As a result of these risks and uncertainties, the amount and composition of the Company's assets, liabilities, officers and/or directors could be significantly different following the outcome of the Chapter 11 Cases, and the description of the Company's operations, properties and liquidity and capital resources included in this quarterly report may not accurately reflect its



operations, properties and liquidity and capital resources following the Debtors' emergence from Chapter 11.

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In particular, subject to certain exceptions, under the Bankruptcy Code, the Debtors may assume, assume and assign or reject executory contracts and unexpired leases subject to the approval of the Bankruptcy Court and certain other conditions. Generally, the rejection of an executory contract or unexpired lease is treated as a pre-petition breach of such executory contract or unexpired lease and, subject to certain exceptions, relieves the Debtors of performing their future obligations under such executory contract or unexpired lease but entitles the contract counterparty or lessor to a pre-petition general unsecured claim for damages caused by such deemed breach subject, in the case of the rejection of unexpired leases of real property, to certain caps on damages. Counterparties to such rejected contracts or leases may assert unsecured claims in the Bankruptcy Court against the applicable Debtor's estate for such damages. Generally, the assumption or assumption and assignment of an executory contract or unexpired lease requires the Debtors to cure existing monetary defaults under such executory contract or unexpired lease and provide adequate assurance of future performance thereunder. Accordingly, any description of an executory contract or unexpired lease with the Debtor in this quarterly report, including where applicable a quantification of the Company's obligations under any such executory contract or unexpired lease with the Debtor is qualified by any overriding rejection rights the Company has under the Bankruptcy Code. Further, nothing herein is or shall be deemed an admission with respect to any claim amounts or calculations arising from the rejection of any executory contract or unexpired lease and the Debtors expressly preserve all of their rights with respect thereto.

See Note 2 Bankruptcy Filing for further information regarding the Chapter 11 Cases.

## **Ability to Continue as a Going Concern**

The Unaudited Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q have been prepared on a going concern basis of accounting, which contemplates continuity of operations, realization of assets, and satisfaction of liabilities and commitments in the normal course of business. The Unaudited Condensed Consolidated Financial Statements do not reflect any adjustments that might result from the outcome of our Chapter 11 Cases. We have significant indebtedness. Our level of indebtedness has adversely impacted and is continuing to adversely impact our financial condition. Our financial condition including operating results, the defaults under our debt agreements, and the risks and uncertainties surrounding our Chapter 11 Cases, raise substantial doubt as to the Company's ability to continue as a going concern.

## **Results of Consolidated Operations**

### **Management Overview**

We are one of the world's leading specialty retailers of fashionable jewelry and accessories for young women, teens, tweens, and kids. Our vision is to be the emporium of choice for all girls (in age or attitude) across the world. We deliver this by offering a range of innovative, fun and affordable products and services that cater to all of her activities, as she grows up, whenever and wherever. Our broad and dynamic selection of merchandise is unique. We are organized into two operating segments: North America and Europe. We identify our operating segments by how we manage and evaluate our business activities. We operate our stores under two brand names: *Claire's*® and *Icing*®. As of August 4, 2018, we operated a total of 2,471 company-operated stores of which 1,466 were located in all 50 states of the United States, Puerto Rico, Canada and the U.S. Virgin Islands (North America segment) and 1,005 stores were located in the United Kingdom, Switzerland, Austria, Germany, France, Ireland, Spain, Portugal, Netherlands, Belgium, Poland, Czech Republic, Hungary, Italy and Luxembourg (Europe segment).

As of August 4, 2018, we also had a total of 6,631 concession stores, of which 6,190 were located in the United States and Canada (North America segment) and 441 stores were located in the United Kingdom, France, Spain, Austria, Germany, Italy, Portugal, Switzerland, Hungary and Poland (Europe segment).



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As of August 4, 2018, we also franchised 687 stores in Japan, the Middle East, Greece, Guatemala, Malta, India, Dominican Republic, El Salvador, Panama, Costa Rica, Romania, Martinique, Pakistan, Thailand, Southern Africa, Russia, Ecuador, Curacao, Chile and Paraguay. We account for the goods we sell to third parties under franchising agreements within Net sales and Cost of sales, occupancy and buying expenses in our Unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss. The franchise fees we charge under the franchising agreements are reported in Other income, net in our Unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss.

*Claire's*® is our primary global brand that we operate through company-operated, concession stores, or franchise stores. *Claire's*® offers a differentiated and fun store experience with a treasure hunt setting that encourages our customer to visit often to explore and find merchandise that appeals to her. We believe by maintaining a highly relevant merchandise assortment and offering a compelling value proposition, *Claire's*® has universal appeal to teens, pre-teens and kids. *Claire's*® target customer is a girl between 3-18 years old for whom we create three distinct ranges: 3 to 6, 6 to 12 and 12 to 18.

*Icing*® is our second brand which we currently operate in North America through company-operated stores and in the Middle East through franchised stores. *Icing*® offers an inspiring merchandise assortment of fashionable products that helps a young woman to say something about herself, whatever the occasion. Our *Icing*® brand targets a young woman in the 18-35 year age group with a focus on our core 21-25 year olds who have recently entered the workforce. This customer is independent, fashion-conscious, and has enhanced spending ability.

We provide our target customer groups with a significant selection of fashionable merchandise across a wide range of categories, all with a compelling value proposition. Our major categories of business are:

Jewelry: Includes earrings as well as our ear piercing service, necklaces, bracelets, body jewelry and rings; and

Accessories: Includes hairgoods; beauty products; room decor; personal, fashion, and seasonal accessories, including tech accessories such as phone cases, jewelry holders, stationery, key rings, attitude glasses, headwear, legwear, armwear, and sunglasses; and handbags and small leather goods.

In North America, our company-operated stores are located primarily in shopping malls. The differentiation of our *Claire's*® and *Icing*® brands allows us to operate multiple stores within a single location. In Europe, our company-operated stores are located primarily on high streets, in shopping malls and in high traffic urban areas.

Financial activity for the three and six months ended August 4, 2018 includes the following:

Net sales decrease of 0.7% and increase of 1.5%; respectively;

Same store sales percentages;

	<b>Three Months Ended August 4, 2018</b>	<b>Six Months Ended August 4, 2018</b>
Consolidated	0.1%	(0.2)%
North America	4.4%	4.9%
Europe	(6.3)%	(8.1)%

Gross profit percentage increase of 180 basis points and 130 basis points, respectively; and

Operating income margin of 11.9% and 10.5%, respectively; excluding \$8.6 million of non-recurring pre-Chapter 11 consulting expense.

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Operational activity for the three and six months ended August 4, 2018 includes the following:

<b>Store Activity Openings (Closings):</b>	<b>Three Months Ended August 4, 2018</b>		<b>Six Months Ended August 4, 2018</b>	
	Opened	Closed <sup>(1)</sup>	Opened	Closed <sup>(1)</sup>
Company-operated	2	(65)	2	(125)
Concession	1,746	(345)	6,119	(458)
Franchise	3	(30)	18	(53)
Total	1,751	(440)	6,139	(636)

(1) Due to underperformance or lease renewal terms of company-operated stores that did not meet our criteria and the cessation of business with certain concession and franchise partners.

A summary of our consolidated results of operations for the three and six months ended August 4, 2018 and July 29, 2017 are as follows (dollars in thousands):

	<b>Three Months Ended August 4, 2018</b>	<b>Three Months Ended July 29, 2017</b>
Net sales	\$ 314,448	\$ 316,637
Increase in same store sales	0.1%	2.8%
Gross profit percentage	50.8%	49.0%
Selling, general and administrative expenses as a percentage of net sales	35.4%	35.6%
Depreciation and amortization as a percentage of net sales	4.4%	3.4%
Operating income	\$ 37,276	\$ 33,172
Net loss	\$ (3,289)	\$ (20,488)
Number of company-operated stores at the end of the period	2,471	2,660
Number of concession stores at the end of the period	6,631	860
	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Net sales	\$ 625,454	\$ 616,258
(Decrease) increase in same store sales	(0.2)%	3.6%
Gross profit percentage	50.4%	49.1%
	37.9%	36.2%

Selling, general and administrative expenses  
as a percentage of net sales (1)

Depreciation and amortization as a percentage of net sales	4.3%	3.6%
Operating income	\$ 57,289	\$ 61,848
Net loss	\$ (14,920)	\$ (27,246)
Number of company-operated stores at the end of the period	2,471	2,660
Number of concession stores at the end of the period	6,631	860

(1) Includes non-recurring pre-Chapter 11 consulting expense of \$8.6 million.

#### *Net sales*

Net sales for the three months ended August 4, 2018 decreased \$2.2 million, or 0.7%, as compared to the three months ended July 29, 2017. Net sales were affected by the effect of company-operated and concession store closures of \$7.9 million, partially offset by a favorable foreign currency translation effect of our non-U.S. net sales of \$3.8 million, an increase in new and same store company-operated sales of \$1.2 million and increased franchisees sales of \$0.7 million. Net sales would have decreased 1.9% excluding the impact of foreign currency exchange rate changes.

Net sales for the six months ended August 4, 2018 increased \$9.2 million, or 1.5%, as compared to the six months ended July 29, 2017. Net sales were affected by a favorable foreign currency translation effect of our non-U.S. net sales of \$18.2 million, an increase in new concession and company-operated store sales of \$2.0 million and increased franchisees sales of \$1.1 million, partially offset by the effect of store closures of \$10.9 million and a decrease in same store sales of \$1.2 million. Net sales would have decreased 1.4% excluding the impact of foreign currency exchange rate changes.

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For the three months ended August 4, 2018, the increase in same store sales was primarily attributable to an increase in average transaction value of 9.7%, partially offset by a decrease in average number of transactions per store of 5.3%. The average transaction value and the average number of transactions are calculated on an average store basis rather than a same store basis.

For the six months ended August 4, 2018, the decrease in same store sales was primarily attributable a decrease in average number of transactions per store of 5.9%, partially offset by an increase in average transaction value of 9.1%. The average transaction value and the average number of transactions are calculated on an average store basis rather than a same store basis.

The following table compares our sales of each product category for each of the periods presented:

<b>Product Category</b>	<b>Percentage of Total Three Months</b>		<b>Percentage of Total</b>	
	<b>Three Months Ended August 4, 2018</b>	<b>Ended July 29, 2017</b>	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Jewelry	49.3	48.5	49.0	48.7
Accessories	50.7	51.5	51.0	51.3
	100.0	100.0	100.0	100.0

*Gross profit*

In calculating gross profit and gross profit percentages, we exclude the costs related to our distribution center and depreciation and amortization expense. These costs are included instead in Selling, general and administrative expenses in our Unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss. Other retail companies may include these costs in cost of sales, so our gross profit percentages may not be comparable to those retailers.

During the three months ended August 4, 2018, gross profit percentage increased 180 basis points to 50.8% compared to 49.0% during the three months ended July 29, 2017. The increase in gross profit percentage consisted of a 100 basis point decrease in occupancy costs and by an 80 basis point increase in merchandise margin. The decrease in occupancy costs, as a percentage of net sales, resulted primarily from cost reductions associated with store closures. The increase in merchandise margin percentage resulted primarily from a favorable foreign currency translation effect.

During the six months ended August 4, 2018, gross profit percentage increased 130 basis points to 50.4% compared to 49.1% during the six months ended July 29, 2017. The increase in gross profit percentage consisted of a 110 basis point decrease in occupancy costs and a 30 basis point increase in merchandise margin, partially offset by a 10 basis point increase in buying and buying-related costs. The decrease in occupancy costs, as a percentage of net sales, resulted primarily from cost reductions associated with store closures. The increase in merchandise margin percentage resulted primarily from a favorable foreign currency translation effect, partially offset by higher markdowns. Markdowns fluctuate based upon many factors, including the amount of inventory purchased versus the rate of sale and promotional activity. We do not anticipate a significant change in the level of markdowns that would materially affect our merchandise margin.



*Selling, general and administrative expenses*

During the three months ended August 4, 2018, selling, general and administrative expenses decreased \$1.3 million, or 1.2%, compared to the three months ended July 29, 2017. As a percentage of net sales, selling, general and administrative expenses decreased 20 basis points compared to the three months ended July 29, 2017. Excluding an unfavorable \$1.4 million foreign currency translation effect, selling, general, and administrative expenses would have decreased by \$2.7 million. Excluding the foreign currency translation effect, the decrease was primarily due to decreased compensation-related expense, including concession store commission expense.

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During the six months ended August 4, 2018, selling, general and administrative expenses increased \$14.0 million, or 6.2%, compared to the six months ended July 29, 2017. As a percentage of net sales, selling, general and administrative expenses increased 170 basis points compared to the six months ended July 29, 2017. Excluding an unfavorable \$7.4 million foreign currency translation effect and non-recurring pre-Chapter 11 consulting expense of \$8.6 million, selling, general, and administrative expenses would have decreased by \$2.0 million. Excluding the foreign currency translation effect and non-recurring pre-Chapter 11 consulting expense of \$8.6 million, the decrease was primarily due to decreased compensation-related expense, including concession store commission expense.

*Depreciation and amortization expense*

During the three months ended August 4, 2018, depreciation and amortization expense increased \$2.8 million to \$13.7 million compared to \$10.9 million for the three months ended July 29, 2017. Excluding an unfavorable \$0.1 million foreign currency translation effect, the increase in depreciation and amortization expense would have been \$2.7 million.

During the six months ended August 4, 2018, depreciation and amortization expense increased \$4.8 million to \$26.9 million compared to \$22.1 million for the six months ended July 29, 2017. Excluding an unfavorable \$0.6 million foreign currency translation effect, the increase in depreciation and amortization expense would have been \$4.2 million.

*Other (income) expense, net*

The following is a summary of other income activity for the three and six months ended August 4, 2018 and July 29, 2017 (in thousands):

	<b>Three Months Ended August 4, 2018</b>	<b>Three Months Ended July 29, 2017</b>	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Royalty income	\$ (2,809)	\$ (2,934)	\$ (5,279)	\$ (5,278)
Foreign currency exchange gain, net	(539)	768	(2,075)	411
Other income		(5)		(5)
	\$ (3,348)	\$ (2,171)	\$ (7,354)	\$ (4,872)

*Reorganization items, net*

Reorganization items, net represent amounts incurred after the Commencement Date as a direct result of the Bankruptcy and are comprised of the following for the three and six months ended August 4, 2018 (in thousands):

	<b>Three Months Ended August 4, 2018</b>	<b>Six Months Ended August 4, 2018</b>
Professional fees	\$ 22,744	\$ 33,697

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Rejection of leases and other	7,277	7,277
Debtor-in-possession financing costs	432	4,470
Write-off of pre-petition debt issuance costs, debt premium, and adjustment in carrying value		(4,982)
Total reorganization items, net	\$ 30,453	\$ 40,462

**Table of Contents***Interest expense, net*

During the three months ended August 4, 2018, net interest expense aggregated \$5.1 million compared to \$43.4 million for the three months ended July 29, 2017. The decrease is primarily due to the cessation of recording interest expense on outstanding debt subject to compromise.

During the six months ended August 4, 2018, net interest expense aggregated \$30.0 million compared to \$87.0 million for the six months ended July 29, 2017. The decrease is primarily due to the cessation of recording interest expense on outstanding debt subject to compromise.

*Income taxes*

The effective income tax rate was 287.8% and (13.6)% for the three and six months ended August 4, 2018. This effective income tax rate differed from the statutory federal income tax rate of 21.0% primarily from foreign losses with no associated income tax benefit and changes in valuation allowances.

The effective income tax rate was (100.4)% and (8.4)% for the three and six months ended July 29, 2017. This effective income tax rate differed from the statutory federal income tax rate of 35% primarily from foreign tax rate differentials as compared to the U.S. statutory rate, changes in the valuation allowance and the correction of an error associated with the prior quarter.

**Segment Operations**

We have two reportable segments North America and Europe. The following is a discussion of results of operations by reportable segment.

*North America*

Key statistics and results of operations for our North America segment are as follows (dollars in thousands):

	<b>Three Months Ended August 4, 2018</b>	<b>Three Months Ended July 29, 2017</b>	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Net sales	\$ 199,454	\$ 196,033	\$ 406,388	\$ 391,993
Increase in same store sales	4.4%	2.6%	4.9%	1.4%
Gross profit percentage	51.8%	48.9%	52.4%	49.9%
Number of company-operated stores at the end of the period	1,466	1,614	1,466	1,614
Number of concession stores at the end of the period	6,190	333	6,190	333

During the three months ended August 4, 2018, net sales in North America increased \$3.4 million, or 1.7%, from the three months ended July 29, 2017. The increase was attributable to an increase in same store and new company-operated store sales of \$8.9 million, increased franchisee sales of \$0.7 million and a favorable foreign currency translation effect of our non-U.S. net sales of \$0.1 million, partially offset by the effect of company-operated and concession store closures of \$6.3 million. Sales would have increased 1.7% excluding the impact from foreign

currency exchange rate changes.

During the six months ended August 4, 2018, net sales in North America increased \$14.4 million, or 3.7%, from the six months ended July 29, 2017. The increase was attributable to an increase in same store sales of \$18.1 million, an increase in new concession and company-operated store sales of \$4.1 million, increased franchisee sales of \$1.1 million and a favorable foreign currency translation effect of our non-U.S. net sales of \$0.6 million, partially offset by the effect of company-operated and concession store closures of \$9.5 million. Sales would have increased 3.5% excluding the impact from foreign currency exchange rate changes.

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For the three months ended August 4, 2018, the increase in same store sales was primarily attributable to an increase in average transaction value of 8.5% and an increase in average number of transactions per store of 1.2%. The average transaction value and the average number of transactions are calculated on an average store basis rather than a same store basis.

For the six months ended August 4, 2018, the increase in same store sales was primarily attributable to an increase in average transaction value of 6.7% and an increase in average number of transactions per store of 1.7%. The average transaction value and the average number of transactions are calculated on an average store basis rather than a same store basis.

During the three months ended August 4, 2018, gross profit percentage increased 290 basis points to 51.8% compared to 48.9% during the three months ended July 29, 2017. The increase in gross profit percentage consisted of a 260 basis point decrease in occupancy costs, a 20 basis point increase in merchandise margin and by a 10 basis point decrease in buying and buying-related costs. The decrease in occupancy costs, as a percentage of net sales, resulted primarily from cost reductions associated with store closures. The increase in merchandise margin percentage resulted primarily from higher initial markups and decreased shrink, partially offset by higher markdowns. Markdowns fluctuate based upon many factors, including the amount of inventory purchased versus the rate of sale and promotional activity. We do not anticipate a significant change in the level of markdowns that would materially affect our merchandise margin.

During the six months ended August 4, 2018, gross profit percentage increased 250 basis points to 52.4% compared to 49.9% during the six months ended July 29, 2017. The increase in gross profit percentage consisted of a 260 basis point decrease in occupancy costs, partially offset by a 10 basis point increase in buying and buying-related costs. The decrease in occupancy costs, as a percentage of net sales, resulted primarily from cost reductions associated with store closures.

The following table compares our sales of each product category in North America for each of the periods presented:

Product Category	Percentage of Total Three Months		Percentage of Total	
	Three Months Ended	Ended	Six Months Ended	Six Months Ended
	August 4, 2018	July 29, 2017	August 4, 2018	July 29, 2017
Jewelry	54.3	54.8	53.8	55.1
Accessories	45.7	45.2	46.2	44.9
	100.0	100.0	100.0	100.0

*Europe*

Key statistics and results of operations for our Europe segment are as follows (dollars in thousands):

Three Months Ended	Three Months Ended	Six Months Ended	Six Months Ended
August 4, 2018	July 29, 2017	August 4, 2018	July 29, 2017

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	<b>2017</b>			
Net sales	\$ 114,994	\$ 120,604	\$ 219,066	\$ 224,265
(Decrease) increase in same store sales	(6.3)%	3.2%	(8.1)%	7.5%
Gross profit percentage	49.1%	49.0%	46.6%	47.8%
Number of company-operated stores at the end of the period	1,005	1,046	1,005	1,046
Number of concession stores at the end of the period	441	527	441	527

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During the three months ended August 4, 2018, net sales in Europe decreased \$5.6 million, or 4.7%, from the three months ended July 29, 2017. The decrease was attributable to a decrease in same stores sales of \$7.7 million, and the effect of company-operated and concession store closures of \$1.6 million, partially offset by a favorable foreign currency translation effect of our non-U.S. net sales of \$3.7 million. Sales would have decreased 7.4% excluding the impact from foreign currency exchange rate changes.

During the six months ended August 4, 2018, net sales in Europe decreased \$5.2 million, or 2.3%, from the six months ended July 29, 2017. The decrease was attributable to a decrease in same stores sales of \$19.2 million and the effect of company-operated and concession store closures of \$3.6 million, partially offset by a favorable foreign currency translation effect of our non-U.S. net sales of \$17.6 million. Sales would have decreased 9.4% excluding the impact from foreign currency exchange rate changes.

For the three months ended August 4, 2018, the decrease in same store sales was primarily attributable to a decrease in average number of transactions per store of 13.0%, partially offset by an increase in average transaction value of 9.2%. The average transaction value and the average number of transactions are calculated on an average store basis rather than a same store basis.

For the six months ended August 4, 2018, the decrease in same store sales was primarily attributable to a decrease in average number of transactions per store of 14.4%, partially offset by an increase in average transaction value of 9.6%. The average transaction value and the average number of transactions are calculated on an average store basis rather than a same store basis.

During the three months ended August 4, 2018, gross profit percentage increased 10 basis points to 49.1% compared to 49.0% during the three months ended July 29, 2017. The increase in gross profit percentage consisted of a 150 basis point increase in merchandise margin and a 10 basis point decrease in buying and buying-related costs, partially offset by a 150 basis point increase in occupancy costs. The increase in merchandise margin percentage resulted primarily from a favorable foreign currency translation effect and lower markdowns, partially offset by lower initial markups. Markdowns fluctuate based upon many factors, including the amount of inventory purchased versus the rate of sale and promotional activity. We do not anticipate a significant change in the level of markdowns that would materially affect our merchandise margin. The increase in occupancy costs, as a percentage of net sales, resulted primarily from the deleveraging effect of a decrease in same store sales.

During the six months ended August 4, 2018, gross profit percentage decreased 120 basis points to 46.6% compared to 47.8% during the six months ended July 29, 2017. The decrease in gross profit percentage consisted of a 210 basis point increase in occupancy costs, partially offset by a 90 basis point increase in merchandise margin. The increase in occupancy costs, as a percentage of net sales, resulted primarily from the deleveraging effect of a decrease in same store sales. The increase in merchandise margin percentage resulted primarily from a favorable foreign currency translation effect and lower markdowns, partially offset by lower initial markups. Markdowns fluctuate based upon many factors, including the amount of inventory purchased versus the rate of sale and promotional activity. We do not anticipate a significant change in the level of markdowns that would materially affect our merchandise margin.

The following table compares our sales of each product category in Europe for each of the periods presented:

Product Category	Percentage of Total		Percentage of Total	
	Three Months Ended	Three Months Ended	Six Months Ended	Six Months Ended



	<b>August 4, 2018</b>	<b>July 29, 2017</b>	<b>August 4, 2018</b>	<b>July 29, 2017</b>
Jewelry	40.8	38.4	40.2	37.7
Accessories	59.2	61.6	59.8	62.3
	100.0	100.0	100.0	100.0

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**Liquidity and Capital Resources**

On March 22, 2018, the Company, entered into a Credit Agreement (the "DIP Credit Agreement") among the Company, Claire's Inc., a Delaware corporation ("Parent"), certain of the Company's subsidiaries, the lenders from time to time party thereto (the "Lenders") and Citibank, N.A., as administrative agent and collateral agent for the Lenders (in such capacities, the "Administrative Agent"), pursuant to which, among other things, the Lenders have provided (i) a senior secured superpriority non-amortizing asset-based revolving facility in an aggregate principal amount of \$75,000,000 (the "DIP ABL Loan"), with up to \$10,000,000 of such DIP ABL Loan available for the issuance of standby letters of credit and (ii) a superpriority senior secured last-out term facility in an aggregate principal amount of \$60,000,000 (the "DIP Term Loan" and together with the DIP ABL Loan, the "DIP Facility").

The proceeds of the DIP ABL Loan were used to refinance all outstanding obligations and replace commitments under the ABL Credit Facility, including cash collateralization of certain letters of credit previously issued, outstanding and undrawn as of March 22, 2018, the closing date of the DIP Facility (the "DIP Closing Date"), and to pay fees, costs and expenses incurred in connection with the DIP Facility. The proceeds of the DIP Facility will also be used for working capital and general corporate purposes and to fund certain fees payable to professional service providers in connection with prosecuting the Chapter 11 Cases.

The Bankruptcy Court has approved the payment of certain pre-petition employee wages and benefits, the use of the debtors' existing cash management system, the maintenance and administration of customer programs, the payment of the pre-petition claims of certain vendors, the honoring of insurance-related obligations, and the payment of certain pre-petition taxes and related fees.

Despite the liquidity provided by our existing cash on hand, our ability to maintain normal credit terms with our suppliers may become impaired. We may be required to pay cash in advance to certain vendors and may experience restrictions on the availability of trade credit, which would further reduce our liquidity. If liquidity problems persist, our suppliers could refuse to provide key products and services in the future. In addition, due to the public perception of our financial condition and results of operations, in particular with regard to our potential failure to meet our debt obligations, some vendors could be reluctant to enter into long-term agreements with us.

In addition to the cash requirements necessary to fund ongoing operations, we have incurred significant professional fees and other costs in connection with our Chapter 11 Cases and expect that we will continue to incur significant professional fees and costs throughout our Chapter 11 Cases.

Although the Company has obtained financing under the DIP Facility, we cannot state with certainty that our liquidity will be sufficient to allow us to satisfy our obligations related to the Chapter 11 Cases or that we will be able to confirm a Chapter 11 plan of reorganization that allows us to emerge from bankruptcy. In addition, we must comply with the covenants of our DIP Facility in order to continue to access our borrowings thereunder. These covenants include, among other things, a minimum EBITDA covenant, restrictions on our ability to, among other things, incur or assume additional debt or provide guarantees in respect of obligations of other persons, prepay, redeem or repurchase subordinated debt, make loans and investments, incur certain liens, impose limitations on dividends, loans or asset transfers from subsidiaries, sell or otherwise dispose of assets, including capital stock of subsidiaries, consolidate or merge with or into, or sell substantially all of its assets to another person and enter into transactions with affiliates, provide financial information, budgets and other information, in each case except as permitted by the applicable agreements governing our DIP Facility. We cannot state with certainty that we will be able to comply with the covenants of our DIP Facility or secure additional interim financing or exit financing sufficient to meet our liquidity needs or, if sufficient funds are available, offered to us on acceptable terms.

Our ability to maintain adequate liquidity through the reorganization process and beyond depends on successful operation of our business, and appropriate management of operating expenses and capital spending. Our anticipated liquidity needs are highly sensitive to changes in each of these and other factors.

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As of August 4, 2018, we had \$65.6 million of availability under the DIP ABL Loan, net of applicable reserves.

Our independent registered public accountants' report dated as of April 20, 2018, includes an other matter paragraph regarding the Company's ability to continue as a going concern. This other matter paragraph constitutes an event of default under the CLSIP Term Loan Agreement that would otherwise permit the lenders under the CLSIP Term Loan to cause such indebtedness to become immediately due and payable. CLSIP Holdings, CLSIP, Wilmington Trust, N.A., as Administrative Agent and Collateral Agent under the CLSIP Term Loan Agreement, and certain of the lenders constituting Required Lenders (as that term is defined by the CLSIP Term Loan Agreement) under the CLSIP Term Loan have entered into a forbearance agreement dated as of April 19, 2018 (the "CLSIP Forbearance") providing that, among other things, such lenders will forbear from causing the CLSIP Term Loan to become immediately due and payable and from exercising remedies arising from such event of default or other events of default that may arise on account of the commencement of the Chapter 11 Cases and/or any other transaction and/or agreement contemplated by the Restructuring Agreement. The CLSIP Forbearance also increased the interest rate of the loan to bear 11.0% per annum. As a result of the CLSIP Forbearance, the CLSIP Term Loan is classified as long-term debt.

Certain indebtedness of our European subsidiaries in an aggregate principal amount of \$85.5 million matures in early 2019, as follows (dollars in millions):

<b>Facility</b>	<b>Outstanding Amount</b>	<b>Maturity</b>
Claire's Gibraltar Credit Facility	\$ 34.0	February 4, 2019
Europe Credit Agreement	\$ 51.5	January 31, 2019

We currently anticipate that our European subsidiaries should be able to refinance this existing indebtedness as it matures, but this will depend on market and other conditions. In addition, efforts to reach agreements on a restructuring of our U.S. debt may impact our ability to refinance the European debt.

A summary of cash flows provided by (used in) operating, investing and financing activities for the six months ended August 4, 2018 and July 29, 2017 is outlined in the table below (in thousands):

	<b>Six Months Ended August 4, 2018</b>	<b>Six Months Ended July 29, 2017</b>
Operating activities	\$ 26,905	\$ (33,233)
Investing activities	(9,127)	(8,139)
Financing activities	13,007	16,566

*Cash flows from operating activities*

For the six months ended August 4, 2018, cash provided by operations increased \$60.1 million compared to the prior year period. The primary reason for the increase provided by operations was an increase in operating income and net other items of \$85.8 million, offset by an increase in working capital of \$25.7 million, excluding cash equivalents. For the six months ended July 29, 2017, cash used in operations decreased \$20.3 million compared to the prior year period. The primary reason for the decrease in cash used in operations was an increase in operating income and net other items of \$28.8 million, offset by an increase in working capital of \$8.5 million, excluding cash equivalents.



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### *Cash flows from investing activities*

For the six months ended August 4, 2018, cash used in investing activities was \$9.1 million and consisted of \$9.1 million for capital expenditures. For the six months ended July 29, 2017, cash used in investing activities was \$8.1 million and consisted of \$8.1 million for capital expenditures.

### *Cash flows from financing activities*

For the six months ended August 4, 2018, cash provided by financing activities was \$13.0 million, which consisted primarily of proceeds from the issuance of our \$60.0 million DIP term loan, partially offset by net payments of \$31.0 million under our ABL Credit Facility, payment of \$5.3 million for unamortized interest related to long-term debt, payment of \$4.5 million in financing costs, payment of \$6.0 million for current portion of long-term debt and payment of \$0.2 million for a capital lease. For the six months ended July 29, 2017, cash provided by financing activities was \$16.6 million, which consisted primarily of net borrowings of \$39.8 million under our ABL Credit Facility, partially offset by payment of \$18.4 million for the extinguishment of the Senior Subordinated Notes, payment of \$4.3 million for unamortized interest related to long-term debt, payment of \$0.4 million in financing costs and payment of \$0.1 million for a capital lease.

We or our affiliates have purchased and may, from time to time, purchase portions of our indebtedness. All of our purchases have been open market transactions.

### *Cash Position*

As of August 4, 2018, we had cash of \$69.4 million.

In addition, as of August 4, 2018, our foreign subsidiaries held cash and cash equivalents of \$35.1 million. During the six months ended August 4, 2018, we transferred certain cash held by foreign subsidiaries to the U.S. to meet certain liquidity needs.

### **ABL Credit Facility**

In March 2018, the Company paid an aggregate amount of \$71.0 million and, in addition, the related accrued interest associated with the extinguishment of the ABL Credit Facility. As a result, the Company discharged all obligations with respect to the Company's ABL Credit Facility.

### *Debt Covenants*

Our debt agreements also contain various covenants that limit our ability to engage in specified types of transactions. These covenants, subject to certain exceptions and other basket amounts, limit our and our subsidiaries' ability to, among other things:

incur additional indebtedness;

pay dividends or distributions on our capital stock, repurchase or retire our capital stock and redeem, repurchase or defease any subordinated indebtedness;

make certain investments;

create or incur certain liens;

create restrictions on the payment of dividends or other distributions to us from our subsidiaries;

transfer or sell assets;

engage in certain transactions with our affiliates; and

merge or consolidate with other companies or transfer all or substantially all of our assets.

For a description of our existing debt and debt agreements, see Note 5 Debt, in the Unaudited Condensed Consolidated Financial Statements. As of August 4, 2018, we were in compliance with the covenants in all existing debt agreements for debt not subject to compromise.

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See Note 4 Fair Value Measurements for related fair value disclosure on debt.

### *Europe Bank Credit Facilities*

Our non-U.S. subsidiaries have bank credit facilities totaling \$1.9 million. These facilities are used for working capital requirements, letters of credit and various guarantees. These credit facilities have been arranged in accordance with customary lending practices in their respective countries of operation. As of August 4, 2018, we had a reduction of \$1.7 million for outstanding bank guarantees, which reduces the borrowing availability to \$0.2 million as of that date.

### *Management Services Agreement*

See Note 10 Related Party Transactions, in the Unaudited Condensed Consolidated Financial Statements.

## **Critical Accounting Policies and Estimates**

Our Unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles. Preparation of these statements requires management to make judgments and estimates. Some accounting policies have a significant impact on amounts reported in these financial statements. A summary of significant accounting policies and a description of accounting policies that are considered critical may be found in our Fiscal 2017 Annual Report on Form 10-K, filed on April 20, 2018, in the Notes to Consolidated Financial Statements, Note 2 Summary of Significant Accounting Policies, and the Critical Accounting Policies and Estimates section contained in the Management's Discussion and Analysis of Financial Condition and Results of Operations therein.

Goodwill and indefinite-lived intangible assets are subject to impairment assessments at least annually (or more frequently when events or circumstances indicate that an impairment may have occurred) by applying a fair-value test. These fair value estimates require significant management judgment and are based on the best information available at the time of the analysis. Our principal intangible assets, other than goodwill, are tradenames, franchise agreements, and leases that existed as of the date that the Company was acquired in May 2007, which had terms that were favorable to market at that date. Our impairment testing for Fiscal 2017 resulted in the recognition of a non-cash impairment charge of \$1.4 million relating to long-lived assets. We expect to next perform our annual impairment analysis during the fourth fiscal quarter of Fiscal 2018, and we may be required to recognize additional impairment charges at that time or in the future.

## **Recent Accounting Pronouncements**

See Note 3 Recent Accounting Pronouncements, in the Notes to the Unaudited Condensed Consolidated Financial Statements.

## **Cautionary Note Regarding Forward-Looking Statements and Risk Factors**

We and our representatives may from time to time make written or oral forward-looking statements, including statements contained in this and other filings with the Securities and Exchange Commission and in our press releases and reports to stockholders. All statements which address operating performance, events or developments that we expect or anticipate will occur in the future, including statements relating to our future financial performance, business strategy, planned capital expenditures, ability to service our debt, and new store openings for future fiscal years, are forward-looking statements. The forward-looking statements are and will be based on management's then current views and assumptions regarding future events and operating performance, and we assume no obligation to update any



forward-looking statement. The forward-looking statements may use the words expect, anticipate, plan, intend, project, may, believe, forecast, and similar expressions. Forward-looking statements involve known or unknown risks, uncertainties and other factors, including changes in estimates and judgments discussed under Critical Accounting Policies and Estimates which may cause our actual results,

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performance or achievements, or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Some of these risks, uncertainties and other factors are as follows: our level of indebtedness; general economic conditions; changes in consumer preferences and consumer spending; unwillingness of vendors and service providers to supply goods or services pursuant to historical customary credit arrangements; competition; general political and social conditions such as war, political unrest and terrorism; natural disasters or severe weather events; currency fluctuations and exchange rate adjustments; failure to maintain our favorable brand recognition; failure to successfully market our products through other channels, such as e-commerce; uncertainties generally associated with the specialty retailing business, such as decreases in mall traffic; disruptions in our supply of inventory; inability to increase same store sales; inability to renew, replace or enter into new store leases on favorable terms; increase in our cost of merchandise; significant increases in our merchandise markdowns; inability to grow our company-operated store base, expand our international store base through franchise or similar licensing arrangements, or expand our store base through concession stores; inability to design and implement new information systems; data security breaches of confidential information or other cyber-attacks; delays in anticipated store openings or renovations; results from any future asset impairment analysis, changes in applicable laws, rules and regulations, including laws and regulations governing the sale of our products, particularly regulations relating to heavy metal and chemical content in our products; changes in anti-bribery laws; changes in employment laws, including laws relating to overtime pay, tax laws and import laws; product recalls; loss of key members of management; increases in the costs of healthcare for our employees; increases in the cost of labor; labor disputes; increases in the cost of borrowings; unavailability of additional debt or equity capital; and the impact of our substantial indebtedness on our operating income and our ability to grow. In addition, we typically earn a disproportionate share of our operating income in the fourth quarter due to seasonal buying patterns, which are difficult to forecast with certainty. Risks and uncertainties relating to any capital restructuring initiative include: risks and uncertainties relating to the Chapter 11 Cases, including but not limited to, the Company's ability to obtain Bankruptcy Court approval with respect to motions filed in the Chapter 11 Cases, the effects of the Chapter 11 Cases on the Company and on the interests of various constituents, Bankruptcy Court rulings in the Chapter 11 Cases and the outcome of the Chapter 11 Cases in general, the length of time the Company will operate as a debtor in possession in Chapter 11, risks associated with motions filed and relief sought by third parties in the Chapter 11 Cases, the potential adverse effects of the Chapter 11 Cases on the Company's liquidity or results of operations or business prospects and increased legal and other professional costs necessary to execute the Company's reorganization; risks and uncertainties associated with the transactions contemplated in the DIP Credit Agreement, Backstop Agreement and Restructuring Support Agreement, including satisfaction of the conditions thereto are subject to certain conditions, which conditions may not be satisfied for various reasons, including for reasons outside of the Company's control, including the negotiation of terms, conditions and provisions related thereto; the ability of the Company to obtain requisite support for the restructuring and a Chapter 11 plan of reorganization from various stakeholders; the ability of the Company to continue as a going concern; the ability of the Company and its Debtor affiliates to confirm a Chapter 11 plan of reorganization; and the effects of disruption from the Chapter 11 Cases and any restructuring transactions pursued or consummated in connection therewith or relating thereto, making it more difficult to maintain business, financing and operational relationships, to obtain and maintain normal terms with customers, suppliers and service providers and to retain key executives and to maintain various licenses and approvals necessary for the Company to conduct its business. The Company undertakes no obligation to update or revise any forward-looking statements to reflect subsequent events or circumstances. Additional discussion of these and other risks and uncertainties is contained elsewhere in this Item 2, in Item 3, Quantitative and Qualitative Disclosures About Market Risk and in our Form 10-K for Fiscal 2017 under Statement Regarding Forward-Looking Disclosures and Risk Factors.

**Table of Contents****Item 3. Quantitative and Qualitative Disclosures About Market Risk***Cash*

We have significant amounts of cash at financial institutions that are in excess of federally insured limits. We cannot be assured that we will not experience losses on our deposits. We mitigate this risk by maintaining bank accounts with a group of credit worthy financial institutions.

*Interest Rates*

As of August 4, 2018, we had fixed rate debt of \$2,066.7 million and variable rate debt of \$94.0 million. Based on our variable rate balance as of August 4, 2018, a 1% change in interest rates would increase or decrease our annual interest expense by approximately \$0.9 million.

*Foreign Currency*

We are exposed to market risk from foreign currency exchange rate fluctuations on the United States dollar ( USD or dollar ) value of foreign currency denominated transactions and our investments in foreign subsidiaries. We manage this exposure to market risk through our regular operating and financing activities, and may from time to time, use foreign currency hedges. Exposure to market risk for changes in foreign currency exchange rates relates primarily to our foreign operations buying, selling, and financing in currencies other than local currencies and to the carrying value of net investments in foreign subsidiaries. As of August 4, 2018, we maintained no foreign currency options. We generally do not hedge the translation exposure related to our net investment in foreign subsidiaries. Included in Comprehensive loss are \$(15.1) million and \$14.0 million, net of tax, reflecting the unrealized gain on foreign currency translations and intra-entity foreign currency transactions during the six months ended August 4, 2018 and July 29, 2017, respectively.

Certain of our subsidiaries make significant USD purchases from Asian suppliers, particularly in China. Until July 2005, the Chinese government pegged its currency, the yuan renminbi ( RMB ), to the USD, adjusting the relative value only slightly and on infrequent occasion. Many people viewed this practice as leading to a substantial undervaluation of the RMB relative to the USD and other major currencies, providing China with a competitive advantage in international trade. China now allows the RMB to float to a limited degree against a basket of major international currencies, including the USD, the euro and the Japanese yen. The official exchange rate has historically remained stable; however, there are no assurances that this currency exchange rate will continue to be as stable in the future due to the Chinese government's adoption of a floating rate with respect to the value of the RMB against foreign currencies. While the international reaction to the RMB revaluation has generally been positive, there remains significant international pressure on China to adopt an even more flexible and more market-oriented currency policy that allows a greater fluctuation in the exchange rate between the RMB and the USD. This floating exchange rate, and any appreciation of the RMB that may result from such rate, could have various effects on our business, which include making our purchases of Chinese products more expensive. If we are unable to negotiate commensurate price decreases from our Chinese suppliers, these higher prices would eventually translate into higher costs of sales, which could have a material adverse effect on our results of operations.

The results of operations of our foreign subsidiaries, when translated into U.S. dollars, reflect the average foreign currency exchange rates for the months that comprise the periods presented. As a result, if foreign currency exchange rates fluctuate significantly from one period to the next, results in local currency can vary significantly upon translation into U.S. dollars. Accordingly, fluctuations in foreign currency exchange rates, most notably the strengthening of the dollar against the euro, could have a material impact on our revenue growth in future periods.



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**Table of Contents***General Market Risk*

Our competitors include department stores, specialty stores, mass merchandisers, discount stores and other retail and internet channels. Our operations are impacted by consumer spending levels, which are affected by general economic conditions, consumer confidence, employment levels, availability of consumer credit and interest rates on credit, consumer debt levels, consumption of consumer staples including food and energy, consumption of other goods, adverse weather conditions and other factors over which we have little or no control. The increase in costs of such staple items has reduced the amount of discretionary funds that consumers are willing and able to spend for other goods, including our merchandise. Should there be continued volatility in food and energy costs, recession in the United States and Europe, rising unemployment and continued declines in discretionary income, our revenue and margins could be significantly affected in the future. We cannot predict whether, when or the manner in which the economic conditions described above will change. See also Cautionary Note Regarding Forward Looking Statements and Risk Factors.

**Item 4. Controls and Procedures***Disclosure Controls and Procedures*

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934), as of the end of the period covered by this Quarterly Report. Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including each of such officers as appropriate to allow timely decisions regarding required disclosure.

*Changes in Internal Controls over Financial Reporting*

No changes in our internal control over financial reporting have been made during the quarter ended August 4, 2018, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

We are, from time to time, involved in routine litigation incidental to the conduct of our business, including litigation instituted by persons injured upon premises under our control; litigation regarding the merchandise that we sell, including product and safety concerns regarding heavy metal and chemical content in our merchandise; litigation with respect to various employment matters, including wage and hour litigation; litigation with present or former employees; and litigation regarding intellectual property rights. Although litigation is routine and incidental to the conduct of our business, like any business of our size which employs a significant number of employees and sells a significant amount of merchandise, such litigation can result in large monetary awards when judges, juries or other finders of facts do not agree with management's evaluation of possible liability or outcome of litigation. In the opinion of management, we believe that current pending litigation will not have a material adverse effect on our consolidated financial results.

See Note 2 Bankruptcy Filing for a description of the Chapter 11 Cases.

Notwithstanding the foregoing, any litigation pending against the Company or any of the Debtors as of the Commencement Date and any claims that could be asserted against the Company or any of the Debtors that arose prior to the Commencement Date are automatically stayed as a result of the commencement of the Chapter 11 Cases pursuant to section 362 of the Bankruptcy Code, subject to certain statutory exceptions. These matters will be subject to resolution in accordance with the Bankruptcy Code and applicable orders of the Bankruptcy Court.

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**Item 1A. Risk Factors**

There have been no material changes in our risk factors disclosed in our Annual Report on Form 10-K for the year ended February 3, 2018.

**Item 6. Exhibits**

10.1	<u>Amendment to Restructuring Support Agreement. (1)</u>
31.1	<u>Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a). (1)</u>
31.2	<u>Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a). (1)</u>
32.1	<u>Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)</u>
32.2	<u>Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)</u>
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

<sup>(1)</sup> Filed herewith.

**Items 2, 3, 4 and 5 of Part II are not applicable and have been omitted.**

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**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.

CLAIRE S STORES, INC.

September 14, 2018

By: /s/ Ron Marshall  
Ron Marshall, Chief Executive Officer (principal executive officer)

September 14, 2018

By: /s/ Scott Huckins  
Scott Huckins, Executive Vice President and Chief Financial Officer (principal financial officer)