

CHEROKEE INC
Form 10-Q
September 08, 2011
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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 July 30, 2011.

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Transition Period From _____ to _____.

Commission file number 0-18640

CHEROKEE INC.

(Exact name of registrant as specified in its charter)

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Delaware

(State or other jurisdiction of Incorporation or organization)

95-4182437

(IRS employer identification number)

6835 Valjean Avenue, Van Nuys, CA

(Address of principal executive offices)

91406

Zip Code

Registrant's telephone number, including area code **(818) 908-9868**

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

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

Class	Outstanding at September 8, 2011
Common Stock, \$.02 par value per share	8,438,566

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CHEROKEE INC.

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	July 30, 2011	January 29, 2011
Assets		
Current assets:		
Cash and cash equivalents	\$ 10,466,000	\$ 9,587,000
Receivables	6,131,000	6,644,000
Income taxes receivable	276,000	1,378,000
Prepaid expenses and other current assets	159,000	94,000
Deferred tax asset	651,000	1,240,000
Total current assets	17,683,000	18,943,000
Deferred tax asset	1,357,000	1,344,000
Property and equipment, net	263,000	173,000
Trademarks, net	6,202,000	6,709,000
Other assets	22,000	14,000
Total assets	\$ 25,527,000	\$ 27,183,000
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 1,841,000	\$ 1,867,000
Accrued compensation payable	76,000	4,314,000
Income taxes payable	486,000	1,010,000
Accrued dividends	1,690,000	1,699,000
Deferred tax liability current	56,000	
Promissory note		7,260,000
Short term debt	3,333,000	
Total current liabilities	7,482,000	16,150,000
Long term liabilities:		
Deferred tax liability non current	38,000	
Long term debt	5,139,000	
Total liabilities	12,659,000	16,150,000
Commitments and Contingencies (Note 6)		
Stockholders Equity		
Preferred stock, \$.02 par value, 1,000,000 shares authorized, none issued and outstanding		
Common stock, \$.02 par value, 20,000,000 shares authorized, 8,494,716 issued and outstanding at July 30, 2011 and 8,896,154 issued and 8,496,154 outstanding at January 29, 2011	169,000	177,000
Additional paid-in capital	19,167,000	18,517,000
Retained earnings (deficit)	(6,468,000)	(401,000)
Less: Treasury Stock, Common: 400,000 shares		(7,260,000)
Total stockholders equity	12,868,000	11,033,000

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Total liabilities and stockholders' equity	\$	25,527,000	\$	27,183,000
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See the accompanying notes which are an integral part of these consolidated financial statements.

Table of Contents**CHEROKEE INC.****CONSOLIDATED STATEMENTS OF OPERATIONS****Unaudited**

	Three months ended		Six months ended	
	July 30, 2011	July 31, 2010	July 30, 2011	July 31, 2010
Royalty Revenue	\$ 6,658,000	\$ 7,496,000	\$ 13,602,000	\$ 15,735,000
Selling, general and administrative	3,954,000	3,363,000	7,258,000	6,731,000
Operating income	2,704,000	4,133,000	6,344,000	9,004,000
Other income:				
Interest expense	(68,000)		(134,000)	
Interest income	2,000	3,000	22,000	7,000
Total other income	(66,000)	3,000	(112,000)	7,000
Income before income taxes	2,638,000	4,136,000	6,232,000	9,011,000
Income tax provision (benefit)	966,000	1,655,000	1,309,000	3,617,000
Net income	\$ 1,672,000	\$ 2,481,000	\$ 4,923,000	\$ 5,394,000
Basic earnings per share	\$ 0.20	\$ 0.28	\$ 0.58	\$ 0.61
Diluted earnings per share	\$ 0.20	\$ 0.28	\$ 0.58	\$ 0.61
Weighted average shares outstanding				
Basic	8,504,247	8,814,187	8,501,867	8,814,187
Diluted	8,534,518	8,855,957	8,528,301	8,848,696

See the accompanying notes which are an integral part of these consolidated financial statements.

Table of Contents**CHEROKEE INC.****CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY****Unaudited**

	Common Stock Shares	Common Stock Par Value	Treasury Stock	Additional Paid-in Capital	Retained Earnings (Deficit)	Total
Balance at January 29, 2011	8,496,154	\$ 177,000	(7,260,000) \$	18,517,000 \$	(401,000) \$	11,033,000
Stock-based compensation				389,000		389,000
Stock options exercised	10,000			161,000		161,000
Stock expirations				(52,000)		(52,000)
Stock issuance	12,562			200,000		200,000
Stock repurchases	(24,000)		(395,000)			(395,000)
Stock retirement		(8,000)	7,655,000	(48,000)	(7,599,000)	
Accrued and unpaid dividends					(3,391,000)	(3,391,000)
Net income					4,923,000	4,923,000
Balance at July 30, 2011	8,494,716	\$ 169,000	\$	19,167,000 \$	(6,468,000) \$	12,868,000

See the accompanying notes which are an integral part of these consolidated financial statements.

Table of Contents**CHEROKEE INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****Unaudited**

	July 30, 2011	July 31, 2010
<u>Operating activities</u>		
Net income	\$ 4,923,000	\$ 5,394,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	43,000	38,000
Amortization of trademarks	681,000	738,000
Deferred income taxes	656,000	136,000
Stock-based compensation	389,000	269,000
Changes in current assets and liabilities:		
Increase in accounts receivable	513,000	245,000
Increase in prepaid expenses and other assets	(73,000)	(47,000)
Decrease (increase) in income taxes receivable	1,102,000	(2,000)
Decrease (increase) in accounts payable	(26,000)	339,000
Decrease in accrued compensation	(4,238,000)	(1,528,000)
Decrease in income taxes payable and other accrued liabilities	(562,000)	(823,000)
Net cash provided by operating activities	3,408,000	4,759,000
<u>Investing activities</u>		
Purchase of property and equipment	(133,000)	(17,000)
Purchase of trademarks, registration and renewal costs	(174,000)	(171,000)
Net cash used in investing activities	(307,000)	(188,000)
<u>Financing activities</u>		
Proceeds from term loan	10,000,000	
Payment of term loan	(1,537,000)	
Proceeds from exercise of stock options	161,000	
Issuance of common stock	200,000	
Repurchase of common stock	(395,000)	
Payment of short term notes payable	(7,260,000)	
Payment of Dividends	(3,391,000)	(6,698,000)
Net cash used in financing activities	(2,222,000)	(6,698,000)
Increase (Decrease) in cash and cash equivalents	879,000	(2,127,000)
Cash and cash equivalents at beginning of period	9,587,000	9,419,000
Cash and cash equivalents at end of period	\$ 10,466,000	\$ 7,292,000
Cash paid during period for:		
Income taxes	\$ 1,914,000	\$ 3,965,000
Declaration of dividends	\$ 1,690,000	\$ 3,349,000

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See the accompanying notes which are an integral part of these consolidated financial statements.

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CHEROKEE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation

The accompanying unaudited condensed consolidated financial statements as of July 30, 2011 and for the three and six month periods ended July 30, 2011 and July 31, 2010 have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). These consolidated financial statements have not been audited by independent registered public accountants but include all adjustments, consisting of normal recurring accruals, which in the opinion of management of Cherokee Inc. (Cherokee or the Company) are necessary for a fair statement of the financial position and the results of operations for the periods presented. The accompanying consolidated balance sheet as of January 29, 2011 has been derived from audited consolidated financial statements, but does not include all disclosures required by GAAP. The results of operations for the three and six month period ended July 30, 2011 are not necessarily indicative of the results to be expected for the fiscal year ending January 28, 2012. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended January 29, 2011.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of sales and expenses during the reporting period. Actual results could differ from those estimates.

As used herein, the term First Quarter refers to the three months ended April 30, 2011; the term Second Quarter refers to the three months ended July 30, 2011; the term Six Months refers to the six months ended July 30, 2011; the term Fiscal 2012 refers to our fiscal year ending January 28, 2012; the term Fiscal 2011 refers to our most recent past fiscal year ended January 29, 2011; the term Fiscal 2010 refers to our past fiscal year ended January 30, 2010.

(2) Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, SPELL C. LLC, a Delaware limited liability corporation. All significant intercompany accounts and transactions have been eliminated in consolidation.

Revenue Recognition

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Revenues from royalty and brand representation agreements are recognized when earned by applying contractual royalty rates to quarterly point of sale data received from our licensees. Our royalty recognition policy provides for recognition of royalties in the quarter earned, although a large portion of such royalty payments are actually received during the month following the end of a quarter. Revenues are not recognized unless collectability is reasonably assured. Certain royalty agreements that account for the majority of our historical revenues are structured to provide royalty rate reductions once certain cumulative levels of sales are achieved by our licensees. Revenue is recognized by applying the reduced contractual royalty rates prospectively to point of sale data as required sales thresholds are exceeded. The royalty rate reductions do not apply retroactively to sales since the beginning of the fiscal year, and as a consequence such royalty rate reductions do not impact previously recognized royalty revenue.

As a result, our royalty revenues from retail sales of branded products by our most significant licensee, Target, as well as certain of our other licensees, are highest at the beginning of each fiscal year and decrease in each fiscal quarter as licensees reach certain retail sales thresholds contained in their respective license agreements.

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Therefore, the amount of royalty revenue we recognize in any quarter is dependent not only on the retail sales of branded products in such quarter but also the royalty rate in effect after considering the cumulative level of retail sales. Historically, this has usually caused our first quarter to be our highest revenue and profitability quarter; our second quarter to be our next highest quarter, and our third and fourth quarters to be our lowest quarters. However, such historical patterns may vary in the future, depending upon the product mix and retail sales volumes achieved in each quarter with our licensees.

Earnings Per Share Computation

The following table provides a reconciliation of the numerator and denominator of the basic and diluted per-share computations for the three and six month periods ended July 30, 2011 and July 31, 2010:

	July 30, 2011		July 31, 2010	
	3 Months	6 Months	3 Months	Six Months
Numerator:				
Net income-numerator for net income per common share and net income per common share assuming dilution	\$ 1,672,000	\$ 4,923,000	\$ 2,481,000	\$ 5,394,000
Denominator:				
Denominator for net income per common share weighted average Shares	8,504,247	8,501,867	8,814,187	8,814,187
Effect of dilutive securities:				
Stock options	30,271	26,434	41,770	34,509
Denominator for net income per common share, assuming dilution:				
Adjusted weighted average shares and assumed exercises	8,534,518	8,528,301	8,855,957	8,848,696

The diluted weighted average number of shares for the three month periods ended July 30, 2011 and July 31, 2010 excludes 637,000 and 160,778, respectively, shares of common stock issuable on the exercise of stock options that have an exercise price above the average market price (anti-dilutive) for the period because such stock options outstanding were anti-dilutive. The diluted weighted average number of shares for the six month periods ended July 30, 2011 and July 31, 2010, respectively, excludes 637,000 and 199,649 shares, respectively, of common stock issuable on the exercise of stock options because such options were anti-dilutive.

Significant Contracts

Our two most significant contracts are our retail direct licensing agreements with Target Stores, a subsidiary of Target Corp. (Target) for the Cherokee brand in the United States, and with Great Britain's Tesco Stores Limited (Tesco) for the Cherokee brand in the United Kingdom, and certain countries in Central Europe, as further described below.

In 1997, we entered into an agreement with Target that grants Target the exclusive right in the United States to use the Cherokee trademarks in certain categories of merchandise. The current terms of our relationship with Target are set forth in a restated license agreement with Target,

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which was entered into effective as of February 1, 2008 (the Restated Target Agreement). The Restated Target Agreement grants Target the exclusive right in the United States to use the Cherokee trademarks in various specified categories of merchandise. The term of the Restated Target Agreement continues through January 31, 2013. However, the Restated Target Agreement provides that if Target remains current in its payments of the minimum guaranteed royalty of \$9.0 million for the

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preceding fiscal year, then the term of the Restated Target Agreement will continue to automatically renew for successive fiscal year terms provided that Target does not give notice of its intention to terminate the Restated Target Agreement during February of the calendar year prior to termination. Under the Restated Target Agreement, Target has agreed to pay royalties based on a percentage of Target's net sales of Cherokee branded merchandise during each fiscal year ended January 31st, which percentage varies according to the volume of sales of merchandise.

On August 1, 2001, we entered into a retail direct license agreement for the Cherokee brand with Tesco. Tesco was granted the exclusive right to manufacture, promote, sell and distribute a wide range of products bearing our Cherokee brand in the United Kingdom and Ireland and is obligated to pay us a royalty based upon a percentage of its net sales of Cherokee branded products in those countries. In January 2004, we granted Tesco the rights to certain other countries including South Korea, Malaysia, Thailand, Slovakia, and Hungary, and in 2005, we added the rights to Poland and the Czech Republic. In March 2006, Tesco began to sell Cherokee branded products in the Czech Republic, Poland, and Slovakia, and, in July 2006, Tesco began to sell Cherokee branded products in Hungary. The term of the Tesco agreement was recently renewed and now expires on January 31, 2014, and Tesco has several options to extend this term.

We also have other licensing agreements regarding our brands, including with: (i) Zellers for our Cherokee brand in Canada; (ii) Nishimatsuya for our Cherokee brand in Japan; (iii) RT Mart for our Cherokee brand in China; (iv) Arvind for our Cherokee brand in India; (v) Magnit for our Cherokee brand in Russia; (vi) TJX Companies for our Carole Little and St. Tropez-West brands in the U.S. and other select countries; and (vii) a number of other international license agreements for our Cherokee brand. For a more complete description of our license agreements and other commercial agreements, please see our Annual Report on Form 10-K for Fiscal 2011.

Stock-Based Compensation

We currently maintain two equity-based compensation plans: (i) the 2003 Incentive Award Plan as amended in 2006 with the adoption of the 2006 Incentive Award Plan (the "2003 Plan"); and (ii) the 2006 Incentive Award Plan (the "2006 Plan"). Each of these equity based compensation plans provide for the issuance of equity-based awards to officers and other employees and directors, and they have previously been approved by our stockholders. Stock options issued to employees are granted at the market price on the date of grant, generally vest over a three-year period, and generally expire seven to ten years from the date of grant. We issue new shares of common stock upon exercise of stock options.

The 2003 Plan was approved at the June 9, 2003 Annual Meeting of Stockholders, and amended at the June 13, 2006 with the adoption of the 2006 Plan by the Company's Stockholders at the June 2006 Annual Meeting of Stockholders. Under the 2003 Plan, the Company is authorized to grant up to 250,000 shares of common stock in the form of incentive and nonqualified options and restricted stock awards. The maximum number of shares which may be subject to granted under the 2003 Plan to any individual in any calendar year cannot exceed 100,000. The principal purposes of the 2003 Plan are to provide an additional incentive for our directors, employees and consultants to further our growth, development and financial success and to enable us to obtain and retain their services. The Compensation Committee of the Board of Directors or another committee thereof (the "Committee") administers the 2003 Plan with respect to grants to our employees or consultants and the full Board of Directors (the "Board") administers the 2003 Plan with respect to grants to independent directors. Awards under the 2003 Plan may be granted to individuals who are then officers or other employees of Cherokee or any of our present or future subsidiaries. Such awards also may be granted to our consultants selected by the Committee for participation in the 2003 Plan. The 2003 Plan provides that the Committee may grant or issue stock options and restricted stock awards, or any combination thereof. Two types of stock options may be granted under the plan: incentive and non-qualified stock options. In addition, restricted stock may be sold to participants at various prices (but not below par value) and made subject to such restrictions as may be determined by the Board or the Committee. The vesting period and term for options granted under the 2003 Plan shall be set by the Committee, with the term being no greater than 10 years, and the options generally will vest over a specific time period as designated by the Committee upon the awarding of such options. During the First Quarter, we granted to non-employee directors and certain employees stock options with a seven-year term to purchase 30,000 shares of our common stock at an exercise price of \$17.21 per share (the closing price on the date of grant) pursuant to the 2003 Plan. We did not make any grants under the 2003 Plan during the

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Second Quarter. As of July 30, 2011, there were 25,315 shares available for option grants under the 2003 Plan. In the event that any outstanding option under the 2003 Plan expires or is terminated, the shares of common stock allocable to the unexercised portion of the option shall then become available for grant in the future, until the 2003 Plan expires on April 28, 2016.

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The 2006 Plan was approved at the June 2006 Annual Meeting of Stockholders and amended at the June 2010 Annual Meeting of Stockholders, under which the Company is authorized to grant up to 750,000 shares of common stock in the form of incentive and nonqualified options and restricted stock awards. The maximum number of shares that may be subject to grant under the 2006 Plan to any individual in any calendar year cannot exceed 100,000. The principal purposes of the 2006 Plan is to provide an additional incentive for our directors, employees and consultants and its subsidiaries to further our growth development and financial success and to enable us to obtain and retain their services. The Committee administers the 2006 Plan with respect to grants to our employees or consultants and the full Board administers the 2006 Plan with respect to grants to independent directors. Under the 2006 Plan, restricted stock may be sold to participants at various prices (but not below par value) and made subject to such restrictions as may be determined by the Board or Committee. The vesting period and term for options granted under the 2006 Plan shall be set by the Committee, with the term being no greater than 10 years, and the options generally will vest over a specific time period as designated by the Committee upon the awarding of such options. During the First Quarter, we granted to certain employees stock options with a seven-year term to purchase 256,000 shares of our common stock at an exercise price of \$17.21 per share (the closing price on the date of grant) pursuant to the 2006 Plan. We did not make any grants under the 2006 Plan during the Second Quarter. As of July 30, 2011, there were 148,500 shares available for option grants under the 2006 Plan. In the event that any outstanding option granted under the 2006 Plan expires or is terminated, the shares of common stock allocable to the unexercised portion of the option shall then become available for grant in the future, until the 2006 Plan expires on April 28, 2016.

Stock-based compensation expense recognized for the Six Months was \$389,000, as compared to \$269,000 for the comparable period in the prior year.

The estimated fair value of options granted during Fiscal 2012 and Fiscal 2011 was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Fiscal 2012	Fiscal 2011
Expected Dividend Yield	4.65%	7.2%
Expected Volatility	50.28	58.8%
Avg. Risk-Free Rate	1.84%	2.1%
Expected Life (in years)	4.5 to 5.0	4.8

The expected term of the options represents the estimated period of time until exercise and is based on historical experience of similar options, giving consideration to the contractual terms, vesting schedules and expectations of future employee behavior. The expected stock price volatility is based on the historical volatility of our stock price. The risk-free interest rate is based on the U.S. Treasury yield in effect at the time of grant with an equivalent remaining term. The dividend yield is based on the past dividends paid and the current dividend yield at the time of grant.

A summary of activity for the Company's stock options for the Six Month is as follows:

	Shares	Weighted Average Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding, at January 29, 2011	949,444	\$ 18.76		

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Granted	286,000	\$	17.21	
Exercised	(10,000)	\$	16.08	
Canceled/forfeited	(85,444)	\$	21.17	
Outstanding, at July 30, 2011	1,140,000	\$	18.22	4.92 \$
Vested and Exercisable at July 30, 2011	339,325	\$	19.62	3.03 \$
Non-vested and not exercisable at July 30, 2011	800,675	\$	17.62	5.40 \$

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As of July 30, 2011, total unrecognized stock-based compensation expense related to non-vested stock options was approximately \$2,502,000, which is expected to be recognized over a weighted average period of approximately 3.28 years. The total fair value of all options which vested during the Six Months was \$325,000.

Trademarks

During the Second Quarter and Six Months, the Company did not acquire any trademarks, nor were there any trademark acquisitions during the comparable period last year. Trademark registration and renewal fees which were capitalized during the Second Quarter and Six Months totaled \$66,000 and \$174,000, respectively. In comparison, for the second quarter and six months of last year, the total trademark registration and renewal fees capitalized totaled \$47,000 and \$171,000, respectively.

Income Taxes

Income tax expense of \$966,000 was recognized for the Second Quarter, resulting in an effective tax rate of 36.6% in the Second Quarter, as compared to 40.0% in the second quarter of last year and compared to 40.2% for the full year of Fiscal 2011. The tax provision in the First Quarter was offset by a tax benefit of \$1.2 million that resulted from the payment to us of a refund from the California Franchise Tax Board of \$2.0 million, plus interest. The refund related to our fiscal 2004 through fiscal 2008 tax years. Additionally, for tax years beginning in 2011, California provides for the election of a single factor apportionment formula. The effect of this election resulted in a tax provision decrease of approximately \$149,000 during the Six Months.

The Company files U.S. federal and state income tax returns. For our federal income tax returns, the Company is generally no longer subject to tax examinations for fiscal years prior to Fiscal 2011. With limited exception, our significant state tax jurisdictions are no longer subject to examinations by the various tax authorities for fiscal years prior to 2007. Although the outcome of tax audits is always uncertain, we believe that adequate amounts of tax, interest and penalties, if any, have been provided for in our income tax reserve for any adjustments that may result from future tax audits. We recognize interest and penalties, if any, related to unrecognized tax benefits within the provision for income taxes in our consolidated statement of income. As of January 29, 2011 and July 30, 2011, respectively, accrued interest on a gross basis was \$110,000 and \$115,000.

As of January 29, 2011 and July 30, 2011, respectively, the total amount of gross unrecognized tax benefits was approximately \$1.1 million and \$0.7 million, of which approximately \$0.9 and \$0.7 million represents the amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate. It is reasonably possible that \$0.5 million of unrecognized tax benefits may decrease within the next 12 months as a result of settling certain positions. The expected net impact of the changes would not have a significant impact on the results of operations or the financial position of the Company.

Recent Accounting Pronouncements

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In the third quarter of 2009, the Company adopted the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC and collectively, the Codification), which establishes the Codification as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with GAAP. The historical GAAP hierarchy was eliminated and the Codification became the only level of authoritative GAAP, other than guidance issued by the SEC. The FASB will not issue new standards in the form of Statements, FASB Staff Positions or Emerging Issues Task Force Abstracts. Instead, it will issue Accounting Standard Updates (ASUs). ASUs will serve to update the Codification, provide background information about the guidance and provide the bases for conclusions on change(s) in the Codification. The Codification is effective for all financial statements issued for interim and annual periods ending after September 15, 2009. The adoption of the Codification did not have an impact on our consolidated financial statements. However, references to specific accounting standards in the notes to our condensed consolidated financial statements have been changed to refer to the appropriate section of the Codification.

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(3) Dividends

On January 28, 2011, our Board of Directors declared a dividend of \$1.7 million, or \$0.20 per share, which was paid on March 15, 2011. On April 30, 2011, our Board of Directors declared a dividend of \$1.7 million, or \$0.20 per share, which was paid on June 15, 2011 to stockholders of record as of June 1, 2011. On July 28, 2011, our Board of Directors declared a dividend of \$1.7 million, or \$0.20 per share, which is to be paid on September 15, 2011 to stockholders of record as of September 1, 2011.

(4) Related Party Transactions

Amendment to our Employment Agreement with our Chief Executive Officer

On July 27, 2011, the Compensation Committee (the *Committee*) of our Board of Directors approved an amendment (the *Amendment*) to that certain employment agreement, dated as of August 26, 2010, by and between Cherokee and Henry Stupp, our Chief Executive Officer, as previously amended on January 28, 2011 and on April 13, 2011 (as amended to date, the *Employment Agreement*) and to that certain Stock Option Agreement, dated as of August 26, 2010, by and between Cherokee and Mr. Stupp, as previously amended on January 28, 2011 (as amended to date, the *Option*).

Pursuant to the Amendment:

(i) The Employment Agreement, pursuant to which Mr. Stupp purchased 81,967 shares of Cherokee's Common Stock for investment proceeds of \$1,500,000 on August 26, 2010 and which previously required Mr. Stupp to purchase an additional number of Cherokee's Common Stock for investment proceeds of \$400,000 on or before July 31, 2011 and which further required Mr. Stupp to purchase an additional number of Cherokee's Common Stock for investment proceeds of \$400,000 on or before January 31, 2012 (such shares, collectively, the *Subsequent Shares*), was amended to provide that Mr. Stupp is to purchase the Subsequent Shares in four equal installments of \$200,000 on or before August 1, 2011, October 31, 2011, January 31, 2012 and April 30, 2012; and

(ii) The Option, which is exercisable for up to 300,000 shares of Cherokee's Common Stock subject to vesting in annual installments, and which previously required Mr. Stupp to forfeit 75,000 of the shares subject to the Option in each event where Mr. Stupp does not acquire the Subsequent Shares on or before July 31, 2011 and January 31, 2012, respectively, for a total of 150,000 shares subject to the Option subject to forfeiture, was amended to provide that such 150,000 shares subject to the Option shall instead be forfeited in installments of 37,500 in the event that the investments in the Subsequent Shares by Mr. Stupp contemplated by the Amendment do not occur on or before August 1, 2011, October 31, 2011, January 31, 2012 and April 30, 2012, respectively.

The descriptions of the Employment Agreement and the Option were previously reported in Cherokee's Current Reports on Form 8-K, which were filed with the Securities and Exchange Commission (the *Commission*) on September 1, 2010 and January 31, 2011, and in Cherokee's Annual Report on Form 10-K, which was filed with the Commission on April 14, 2011, and is incorporated herein by reference.

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Pursuant to the Employment Agreement, on July 28, 2011, Mr. Stupp purchased 12,562 shares of Cherokee's common stock at a per share price of \$15.92 (which was equal to the closing price of Cherokee's common stock on such date), for aggregate proceeds of approximately \$200,000.

Also on July 27, 2011, the Committee approved the payment of a discretionary bonus to Mr. Stupp in the amount of \$270,000, which was paid in accordance with Cherokee's payroll practices on July 29, 2011.

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Separation of our Former Executive Chairman

On January 28, 2011, Robert Margolis resigned his positions as Executive Chairman and as a director of Cherokee. In connection with Mr. Margolis' resignation from Cherokee, Mr. Margolis and Cherokee entered into a Separation Agreement and General Release of all Claims (the Separation Agreement), dated January 28, 2011. Pursuant to the Separation Agreement: (i) Cherokee repurchased 400,000 shares of common stock from Mr. Margolis' affiliates at a per share price of \$18.15, or \$7.26 million in total; (ii) Cherokee paid Mr. Margolis a one-time lump sum payment of an aggregate of \$2.26 million; (iii) in early April 2011, Mr. Margolis was paid his final annual performance bonus of approximately \$1.8 million for Fiscal 2011 in accordance with the management agreement previously governing the terms of Mr. Margolis' services to us; (iv) the vesting on Mr. Margolis' outstanding option to purchase up to 100,000 shares of Cherokee's Common Stock was accelerated; and (v) the management agreement previously governing the terms of Mr. Margolis' services to us was terminated. The Separation Agreement contains a general and mutual release of claims and covenant not to sue between Cherokee and Mr. Margolis and a mutual non-disparagement covenant, as well as a two year non-solicitation covenant of Mr. Margolis relating to Cherokee's employees. The terms and conditions of the Separation Agreement were approved by a special committee of Cherokee's Board of Directors, comprised of Cherokee's independent directors. As of January 29, 2011 and January 30, 2010, our accrued liabilities include a bonus payable of approximately \$1.8 million and \$2.5 million, respectively, for Mr. Margolis. Mr. Margolis' Fiscal 2011 bonus was paid in early April 2011, and we do not have any further payment obligations to him.

(5) Debt

On February 16, 2011, Cherokee and U.S. Bank National Association (the Bank) entered into a Term Loan Agreement (the Loan Agreement). Pursuant to the Loan Agreement, Cherokee borrowed \$10,000,000 in principal from the Bank (the Loan). The Loan is to be repaid in equal monthly installments of \$277,778 plus interest over three years, with the balance due at maturity, and with interest on the Loan calculated at a floating rate equal to either (i) the Bank's prime rate minus 0.25% or (ii) 2.75% plus the 1, 2 or 3 month LIBOR rate, as selected by Cherokee. The Loan Agreement contains various affirmative and negative covenants that are customary for loan agreements and transactions of this type, including limitations on our ability to incur debt or other liabilities and limitations on our ability to consummate acquisitions in any fiscal year in excess of \$5,000,000 or in excess of \$10,000,000 in the aggregate while the Loan is outstanding. Further, as collateral for the Loan, the Company granted a security interest in favor of the Bank in all of Cherokee's assets, and the Loan is guaranteed by Cherokee's wholly owned subsidiary, Spell C. LLC. Proceeds from the Loan were primarily used to satisfy the Company's promissory note payable to our former Executive Chairman. On September 6, 2011, we entered into an amendment to the Loan Agreement to (i) modify the covenants relating to, and related definitions of, the fixed charge coverage ratio and tangible net worth as such terms are defined in the Amendment, and (ii) modify the covenant relating to the Company's ability to make certain permitted acquisitions under the Loan Agreement, such that the Company is now permitted, subject to certain conditions, to consummate acquisitions in any fiscal year in amounts below \$5,000,000 or in amounts below \$10,000,000 in the aggregate while the Loan is outstanding.

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As of July 30, 2011 and January 29, 2011, outstanding borrowings of the Company consist of the following:

	July 30, 2011	January 29, 2011
Promissory Note to former Executive Chairman		7,260,000
Term Loan	8,472,221	
	8,472,221	7,260,000
Less current portion of long-term debt	(3,333,333)	(7,260,000)
Long-term portion of debt	5,138,888	

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary note regarding forward looking statements

This quarterly report on Form 10-Q and other filings which we make with the Securities and Exchange Commission, as well as press releases and other written or oral statements we may make may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used, the words anticipates, believes, estimates, objectives, goals, aims, hopes, may, likely, similar expressions are intended to identify such forward-looking statements. In particular, the forward-looking statements in this Form 10-Q include, among others, statements regarding our goals or expectations regarding our future revenues and earnings, the likelihood of increased retail sales by our current and future licensees, such as Target and Tesco, the likelihood that our licensees will achieve royalty rate reductions, our prospects for obtaining new licensees and our prospects for obtaining new brands to acquire or represent. Forward-looking statements involve known and unknown risks and uncertainties that may cause our actual results, performance, achievements or share price to be materially different from any future results, performance, achievements or share price expressed or implied by any forward-looking statements. Such risks and uncertainties include, but are not limited to, the financial condition of the apparel industry and the retail industry, the overall level of consumer spending and our exposure to general economic conditions, the effect of intense competition we face from other apparel lines both within and outside of Target and Tesco, adverse changes in licensee or consumer acceptance of products bearing the Cherokee brand or our other brands as a result of fashion trends or otherwise, our ability to protect our intellectual property rights, the ability and/or commitment of our licensees to design, manufacture and market Cherokee or our other branded products, our dependence on two licensees for a substantial portion of our revenues, our dependence on our key management personnel and our recent appointment of our new Chief Executive Officer and our new Chief Financial Officer, any adverse determination of claims, liabilities or litigation, the requirements under our term loan with U.S. Bank, our ability to issue preferred stock with rights and privileges that are superior to those of our common stock, our payment or non-payment of dividends in future periods and the volatility in the trading price of our common stock. Several of these risks and uncertainties are discussed in more detail under Item 1A. Risk Factors in this Report on Form 10-Q or in the discussion and analysis below. You should, however, understand that it is not possible to predict or identify all risks and uncertainties and you should not consider the risks and uncertainties identified by us to be a complete set of all potential risks or uncertainties that could materially affect us. You should not place undue reliance on the forward-looking statements we make herein because some or all of them may turn out to be wrong. We undertake no obligation to update any of the forward-looking statements contained herein to reflect future events and developments.

Introduction

The following discussion should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this Report on Form 10-Q. See Item 1. Consolidated Financial Statements and our Form 10-K for our fiscal year ended January 29, 2011 (Fiscal 2011).

Cherokee Inc. (which may be referred to as we, us, our or the Company) is a global marketer and manager of a portfolio of lifestyle brands it owns or represents, licensing the Cherokee, Sideout and Carole Little brands and related trademarks and other brands in multiple consumer product categories and sectors. We are one of the leading licensors of brand names and trademarks for apparel, footwear, home and accessories in the world.

We own several trademarks, including Cherokee®, Sideout®, Sideout Sport®, Carole Little®, Saint Tropez-West®, Chorus Line®, All That Jazz® and others. As of July 30, 2011, we had thirty-two continuing license agreements covering both domestic and international markets. As part of our business strategy, we frequently evaluate other brands and trademarks for acquisition into our portfolio.

In addition to licensing our own brands, we also assist other brand-owners, companies, wholesalers and retailers in identifying opportunities as a licensee or licensor for their brands or stores.

We have a 52 or 53 week fiscal year ending on the Saturday nearest to January 31, which aligns us with our retailer licensees who generally also operate and plan using such a fiscal year. This results in a 53 week fiscal year approximately every four or five years. We do not believe that the extra week in the occasionally reported 53-week fiscal year results in any material impact on our financial results.

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Critical Accounting Policies and Estimates

Management's discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, management evaluates its estimates, including those related to revenue recognition, deferred taxes, impairment of long-lived assets, contingencies and litigation. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

We consider accounting policies relating to the following areas to be both those most important to the portrayal of our financial condition and those that require the most subjective judgment:

- Revenue recognition;

- Provision for income taxes and deferred taxes;

- Impairment of long-lived assets;

- Contingencies and litigation; and

- Accounting for stock-based compensation.

You should refer to our Annual Report on Form 10-K for Fiscal 2011, for a discussion of our policies on revenue recognition, deferred taxes, impairment of long-lived assets, contingencies and litigation and accounting for stock-based compensation.

Recent Accounting Pronouncements

We describe recent accounting pronouncements in Item 1 Consolidated Financial Statements Notes to Consolidated Financial Statements.

Results of Operations

Retail Sales

During the quarterly period ended July 30, 2011 (the *Second Quarter*), total U.S. dollar based retail sales of merchandise bearing the Cherokee brand were 11.1% below the total U.S. dollar based retail sales for the second quarter of last year, with U.S. dollar based retail sales totaling approximately \$271.9 million in our *Second Quarter* versus approximately \$305.8 million in total U.S. dollar based retail sales for the second quarter of last year. During the six month period ended July 30, 2011 (the *Six Months*), the total U.S. dollar based retail sales of merchandise bearing the Cherokee brand in all licensed territories were 11.7% below the comparable six months period of last year, totaling \$574.2 million in the *Six Months* as compared to \$650.4 million in the comparable period of last year. Most of this decline resulted from a decrease in categories for the Cherokee brand at certain licensees' stores, particularly Tesco, during the *Second Quarter* and during our quarterly period ended April 30, 2011 (the *First Quarter*), as compared to the comparable periods of last year.

Pursuant to our typical arrangements with our licensees, we receive quarterly royalty statements and periodic retail sales information for Cherokee branded products and other product brands that we own or represent. However, our licensees are generally not required to provide, and typically do not provide, information that would enable us to determine the specific reasons for period-to-period fluctuations in retail sales of our branded products by our licensees in the specific territories in which they operate. Fluctuations in retail sales of Cherokee branded products or other product brands that we own or represent may be the result of a variety of factors, including, without limitation: (i) changes in the number of product categories for which a licensee chooses to use our brands from period-to-period, which generally results in changes in the amount of inventory (utilizing our brands) available for sale from period-to-period; (ii) the number of geographical markets/territories or number of stores in which our licensees are currently selling Cherokee or our other branded products from period-to-period; or (iii) our licensees experiencing changes in retail sales levels as a result of a variety of factors, including fashion-related and general retail sales trends (See Item 1A. *Business Risk Factors*).

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During the Second Quarter, retail sales of Cherokee branded products by Target Stores totaled approximately \$148.0 million compared to approximately \$143.6 million for the second quarter of last year, or an increase of 3.1%. As a consequence, our royalty revenues for the Second Quarter from Target Stores increased 2.0% compared to the comparable period last year.

Tesco's U.S. dollar based retail sales of merchandise bearing the Cherokee brand, which for the Second Quarter and last year's comparable period included the U.K., Ireland, Poland, the Czech Republic, Hungary and Slovakia, were \$60.0 million in our Second Quarter, compared to \$113.1 million in the second quarter of last year, representing a total decline of 46.9%. This decline was due to a reduction of Cherokee branded product categories in the UK and Central European countries during the Second Quarter as compared to the second quarter of the prior year. Retail sales in the United Kingdom, as measured in British Pounds Sterling, were down 49.2% in the Second Quarter as compared to the comparable period in the prior year. Hence, retail sales in U.S. dollars for the United Kingdom totaled \$42.3 million in the Second Quarter, as compared to \$76.4 million in the second quarter of last year. The Tesco Central European countries of the Czech Republic, Slovakia, Poland and Hungary, as measured in their respective local currencies, reflected decreases in retail sales ranging from 50% to 52%. As a consequence the collective U.S. dollar based retail sales from Tesco Central Europe for the Second Quarter were \$13.9 million, as compared to \$28.3 million in the second quarter of last year.

Zeller's retail sales of merchandise bearing the Cherokee brand, in U.S. dollars, were approximately \$23.3 million during the Second Quarter compared to \$19.1 million for the second quarter of last year, representing a 22.4% increase. This increase was due to an expansion in product categories for the Cherokee brand.

Despite the difficult retail environment, the fluctuation of the U.S. dollar in the First Quarter and Second Quarter and the decline of product categories for certain licensees, on a U.S. dollar basis we experienced retail sales increases with several other of our smaller licensees, including in the countries of China, Mexico, South Africa, Israel, Chile and India. We expect that several of our licensees may continue to show growth throughout Fiscal 2012 and we expect our licensee in Japan to begin selling Cherokee branded products later this year.

Royalty Revenues and Expenses

Royalty revenues were \$6.7 million and \$13.6 million during the Second Quarter and the Six Months, respectively, which were \$0.8 million and \$2.1 million less than the \$7.5 million and \$15.7 million reported during the comparable periods of last year. Revenues from the Cherokee brand were \$5.7 million and \$11.8 million during the Second Quarter and Six Months, respectively, as compared to \$6.6 million and \$13.8 million for the comparable periods of last year. The decline was principally due to a decrease in royalty revenues from Tesco during the Second Quarter and during the Six Months. During the Second Quarter and Six Months, revenues of \$2.8 million and \$6.6 million, respectively, were recognized from Target Stores compared to \$2.7 million and \$6.5 million for the comparable periods last year. This accounted for 42% and 48% of our total revenues for the Second Quarter and Six Months, respectively, versus 36% and 42% for the comparable periods last year.

Revenues from all of the Tesco countries were \$1.2 million and \$2.1 million during the Second Quarter and Six Months, respectively, compared to \$2.6 million and \$4.9 million for the comparable periods last year. Royalty revenues from Tesco U.K. totaled \$0.8 million and \$1.4 million during the Second Quarter and Six Months, respectively, as compared to \$1.7 million and \$3.3 million for the comparable periods last year. The decline in royalties from Cherokee branded products in all other Tesco countries (Ireland, Central Europe and Turkey) during the Second Quarter and Six Months was about 55.9% and 51.1%, respectively. This resulted in royalties of \$0.4 million and \$0.8 million for the Second Quarter and Six Months, respectively, as compared to \$0.7 million

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and \$1.6 million for the comparable periods of last year. The decrease in royalties from the Central European Tesco territories is due primarily to the decrease in several Cherokee branded product categories for apparel during the Second Quarter and Six Months as compared to the comparable periods of last year.

Revenues from Zellers increased 6.9% and 13.2% during the Second Quarter and Six Months, respectively, resulting in royalties of \$480,000 and \$916,000 compared to \$381,000 and \$774,000 for the comparable periods last year. Royalty revenues from our retail direct licensee in Mexico, Comercial Mexicana, totaled \$207,000 and \$398,000 during the Second Quarter and Six Months, respectively, as compared to \$175,000 and \$333,000 in royalty revenues for the comparable periods of last year.

Second Quarter and Six Months revenues also included \$263,000 and \$500,000, respectively, from TJX (per our licensing contract for the Carole Little brands), as compared to \$315,000 and \$688,000 for the comparable periods last year, due to lower retail sales of Carole Little branded products during the First Quarter and the Second Quarter. Revenues from our brand representation licensing arrangements totaled \$539,000 in our Second Quarter and \$1.1 million in the Six Months, as compared to \$539,000 and \$1.1 million, respectively, in the comparable periods last year.

Revenues from licensees of both Cherokee and Sideout brands, such as Tesco and Zellers, were collectively \$3.0 million and \$5.3 million during the Second Quarter and Six Months compared to \$3.9 million and \$7.4 million for the comparable periods last year. This decrease is primarily due to the decrease in Cherokee branded product categories in Tesco Central Europe and the current difficult retailing environment globally. The Company's products are sold in various countries and the fluctuation of the US dollar compared to the local currency in which the sale is transacted results in either increased or decreased revenues to Cherokee. During the second quarter and the sixth months ended, the overall weakening of the US dollar resulted in increased revenues to the Company.

Royalty revenues during the Second Quarter of Fiscal 2012 benefited from higher royalty rates than the second quarter of Fiscal 2011 pursuant to our contracts with Tesco and Target during the period because the cumulative retail sales during the Second Quarter had not exceeded the applicable thresholds for reduced royalty rates during Fiscal 2012. In the event that cumulative retail sales in future quarters in Fiscal 2012 do exceed the applicable thresholds for reduced royalty rates, we will then be paid at a reduced royalty rate on incremental retail sales by Target and Tesco that are in excess of such thresholds.

We believe that our future revenues from Target, for the remaining six months of Fiscal 2012, will likely be higher when compared to the revenues from Fiscal 2011 during such period, as we expect our presence in certain apparel categories at Target may continue to grow. In January 2011, Target entered into an agreement with Zellers to acquire leasehold interests in approximately 220 stores for \$1.83 billion, allowing Target to open its first stores in Canada beginning in 2013. Target expects to open 150 stores throughout Canada in 2013. Discussions regarding the transition of our agreement with Zellers to Target are in process. Unless and until a new agreement is reached, sales in Canada during Fiscal 2012 will be governed by the contract already in place with Zellers.

Based on Tesco's sales of Cherokee branded products in Fiscal 2011 and the Six Months, we believe that our revenues during the remainder of Fiscal 2012 from Tesco will probably be lower when compared to the revenues from Fiscal 2011.

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We recognize royalty revenues in the quarter earned. A large portion of such royalty revenues recognized as earned are collected from licensees during the month following the end of a quarter. Our trade receivables balance of \$6.1 million as of the end of the Second Quarter included accrual for revenues earned from Target Stores, Zellers, Tesco, TJX and other licensees that are expected to be received in the month or 45 days following the end of the Second Quarter.

Selling, general and administrative expenses for the Second Quarter and Six Months were \$3.95 million and \$7.26 million, or 59.4% and 53.4% of revenues, respectively, in comparison to selling, general and administrative expenses of \$3.36 million and \$6.73 million, or 44.9% and 42.8%, respectively, of revenues during the comparable periods last year. The changes in our selling, general and administrative expenses, including the increase of about \$0.5 million during the Second Quarter as compared to the second quarter of last year, resulted from the following factors: (i) significantly higher marketing and creative service related expenses; (ii) an increase in personnel expenditures from additional hires and a bonus to our Chief Executive Officer; and (iii) the elimination of

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salary and bonus to our former Executive Chairman.

During the Second Quarter and Six Months, our investment and interest income were \$2,000 and \$22,000, respectively, as compared to \$3,000 and \$7,000 for the comparable periods last year.

During the Second Quarter and Six Months, we recorded a tax provision of \$966,000 and \$1,309,000, respectively, which equates to an unusually low effective tax rate of 36.6% and 21%, compared to a tax provision of \$1.7 million and \$3.6 million and a more typical effective tax rate of 40.0% and 40.1%, respectively, and recorded for the comparable periods last year. The tax provision in the First Quarter was offset by a tax benefit of \$1.2 million that resulted from the payment to us of a refund from the California Franchise Tax Board of \$2.0 million plus interest. The refund related to fiscal 2004 through fiscal 2008 tax years, and we do not currently expect to receive similar tax benefits in future periods. During the Second Quarter and Six Months, our net income was \$1.7 million and \$4.9 million, or \$0.20 and \$0.58 per diluted share, respectively, compared to \$2.5 million and \$5.4 million, or \$0.28 and \$0.61 per diluted share, respectively, for the comparable periods last year.

Amendment to our Employment Agreement with our Chief Executive Officer

On July 27, 2011, the Compensation Committee (the *Committee*) of our Board of Directors approved an amendment (the *Amendment*) to that certain employment agreement, dated as of August 26, 2010, by and between Cherokee and Henry Stupp, our Chief Executive Officer, as previously amended on January 28, 2011 and on April 13, 2011 (as amended to date, the *Employment Agreement*) and to that certain Stock Option Agreement, dated as of August 26, 2010, by and between Cherokee and Mr. Stupp, as previously amended on January 28, 2011 (as amended to date, the *Option*).

Pursuant to the Amendment:

(i) The Employment Agreement, pursuant to which Mr. Stupp purchased 81,967 shares of Cherokee's Common Stock for investment proceeds of \$1,500,000 on August 26, 2010 and which previously required Mr. Stupp to purchase an additional number of Cherokee's Common Stock for investment proceeds of \$400,000 on or before July 31, 2011 and which further required Mr. Stupp to purchase an additional number of Cherokee's Common Stock for investment proceeds of \$400,000 on or before January 31, 2012 (such shares, collectively, the *Subsequent Shares*), was amended to provide that Mr. Stupp is to purchase the Subsequent Shares in four equal installments of \$200,000 on or before August 1, 2011, October 31, 2011, January 31, 2012 and April 30, 2012; and

(ii) The Option, which is exercisable for up to 300,000 shares of Cherokee's Common Stock subject to vesting in annual installments, and which previously required Mr. Stupp to forfeit 75,000 of the shares subject to the Option in each event where Mr. Stupp does not acquire the Subsequent Shares on or before July 31, 2011 and January 31, 2012, respectively, for a total of 150,000 shares subject to the Option subject to forfeiture, was amended to provide that such 150,000 shares subject to the Option shall instead be forfeited in installments of 37,500 in the event that the investments in the Subsequent Shares by Mr. Stupp contemplated by the Amendment do not occur on or before August 1, 2011, October 31, 2011, January 31, 2012 and April 30, 2012, respectively.

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The descriptions of the Employment Agreement and the Option were previously reported in Cherokee's Current Reports on Form 8-K, which were filed with the Securities and Exchange Commission (the Commission) on September 1, 2010 and January 31, 2011, and in Cherokee's Annual Report on Form 10-K, which was filed with the Commission on April 14, 2011, and is incorporated herein by reference.

Pursuant to the Employment Agreement, on July 28, 2011, Mr. Stupp purchased 12,562 shares of Cherokee's common stock at a per share price of \$15.92 (which was equal to the closing price of Cherokee's common stock on such date), for aggregate proceeds of approximately \$200,000.

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Liquidity and Capital Resources

Cash Flows. On July 30, 2011, we had cash and cash equivalents of \$10.5 million. On January 29, 2011, we had cash and cash equivalents of \$9.6 million. The \$0.9 million increase in cash and cash equivalents during the Second Quarter is primarily attributable to our receipt of \$2.0 million tax refund plus interest from the California Franchise Tax Board and our receipt of \$10 million from US Bank pursuant to our term loan. This increase was partially offset by the payment to our former Chief Executive Officer of \$7.6 million for the repurchase of common stock and our payment to him of a previously accrued bonus of \$1.8 million during the First Quarter.

During the Six Months, cash provided by our operations was \$3.4 million, compared to cash provided by our operations of \$4.8 million for the six months ended last year. The cash provided by operations of \$3.4 million during the Six Months was primarily due to the changes in: (i) accrued compensation, which was reduced by \$4.2 million in the Six Months, as compared to a decrease of \$1.5 million in the comparable period last year; (ii) accounts receivable, which decreased by \$0.5 million in the Six Months, as compared to an increase of \$0.2 million in the comparable period last year; (iii) a decrease in tax receivable of \$1.1 million in the Six Months, as compared to an increase of \$2,000 in the comparable period last year. In addition, our cash from operations includes non-cash stock-based compensation expense of \$389,000 in the Six Months as compared to \$269,000 in the comparable period last year, and our deferred tax assets decreased by \$656,000 in the Six Months, as compared to a decrease of \$136,000 last year.

Cash used by investing activities during the Six Months was \$307,000, which was comprised of \$133,000 of capital expenditures of office equipment, and \$174,000 in trademark registration and renewal fees for the Cherokee, Sideout and Carole Little brands. In comparison, during the six months ended last year, cash used by investing activities was \$188,000, which was comprised of \$17,000 of capital expenditures of office equipment, and \$171,000 in trademark registration and renewal fees for the Cherokee, Sideout and Carole Little brands.

Cash used in financing activities was \$2.2 million during the Six Months, which consisted of proceeds of \$10 million from the Term Loan, and the investment of \$200,000 by our Chief Executive Officer in our Common Stock pursuant to his employment agreement, offset by payments of \$1.5 million for the Term Loan, the payment of two dividends totaling \$3.4 million and the payment of \$7.6 million for the repurchase and retirement of stock. In comparison, during the comparable period last year cash used in financing activities was \$6.7 million, which consisted of the payment of two dividends during this period.

Uses of Liquidity. We anticipate that our cash requirements through the end of Fiscal 2012 are primarily to fund operations, trademark registration expenses, capital expenditures, selectively expand our brand portfolio and, if adequate, and, at the discretion of our Board, to pay dividends and/or potentially repurchase shares of our common stock. Our Board may reduce or discontinue payment of dividends at any time for any reason deemed relevant. Our dividend payments in certain past quarters have exceeded our cash flow from operations, and our dividends may not continue at current levels in future periods unless cash flow from operations increases. The declaration and payment of any future dividends or repurchase of shares of our common stock will be at the discretion of our Board and will be dependent upon our financial condition, results of operations, cash flow, capital expenditures and other factors deemed relevant by our Board.

We are frequently approached by parties seeking to sell their brands and related trademarks. Should an established marketable brand or equity become available on favorable terms, we would be interested in pursuing such an acquisition and may elect to fund such acquisition, in whole or in part, using our then-available cash.

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Sources of Liquidity. Our primary source of liquidity is expected to be cash flow generated from operations, and cash and cash equivalents currently on hand. We believe our cash flow from operations together with our cash and cash equivalents currently on hand will be sufficient to meet our working capital, capital expenditure and other commitments through April 2012. We cannot predict our revenues and cash flow generated from operations. Some of the factors that could cause our revenues and cash flows to be materially lower are described under the caption titled *Risk Factors* in Item 1A of this Report on Form 10-Q.

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On February 16, 2011 (the Effective Date), Cherokee and U.S. Bank National Association (the Bank) entered into a Term Loan Agreement (the Loan Agreement). Pursuant to the Loan Agreement, on the Effective Date, Cherokee borrowed \$10,000,000 in principal from the Bank (the Loan). The Loan is evidenced by a term note in the principal amount of \$10,000,000, a security agreement, a California judicial reference agreement and a continuing guaranty executed by Cherokee's wholly owned subsidiary, Spell C. LLC (collectively, with the Loan Agreement, the Loan Documents). On September 6, 2011, we entered into an amendment to the Loan Agreement to (i) modify the covenants relating to, and related definitions of, the fixed charge coverage ratio and tangible net worth as such terms are defined in the Amendment, and (ii) modify the covenant relating to the Company's ability to make certain permitted acquisitions under the Loan Agreement, such that the Company is now permitted, subject to certain conditions, to consummate acquisitions in any fiscal year in amounts below \$5,000,000 or in amounts below \$10,000,000 in the aggregate while the Loan is outstanding. As of July 30, 2011, our outstanding principal balance under the Loan Agreement was \$8.5 million.

If our revenues and cash flows during Fiscal 2012 are lower than Fiscal 2011 we would have less cash available to pay dividends, repurchase shares of our common stock or to explore or consummate the acquisition of other brands. In addition, if our revenues and cash flows during Fiscal 2012 are materially lower than Fiscal 2011, we may need to take steps to reduce expenditures by scaling back operations and reducing staff. We believe that we will have sufficient cash generated from our business activities to support our operations for the next twelve months.

Inflation and Changing Prices

Inflation, traditionally, has not had a significant effect on our operations. Since most of our future revenues are based upon a percentage of sales of the licensed products by our licensees, we do not anticipate that short term future inflation will have a material impact, positive or negative, on future financial results.

Seasonality

Given our contractual royalty rate reductions with our licensees, as certain sales volume thresholds are achieved by our licensees in any given fiscal year, historically this has usually caused our first quarter to be our highest revenue and profitability quarter; our second quarter to be our next highest quarter, and our third and fourth quarters to be our lowest quarters. However, such historical patterns may vary in the future, depending upon the product mix and retail sales volumes achieved in each quarter with our licensees.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Market risk generally represents the risk that losses may occur in the values of financial instruments as a result of movements in interest rates, foreign currency exchange rates and commodity prices. We do not enter into derivatives or other financial instruments for trading or speculative purposes.

Interest: From time to time we invest our excess cash in interest-bearing temporary investments of high-quality issuers. Due to the short time the investments are outstanding and their general liquidity, these instruments are classified as cash equivalents in our consolidated balance sheet

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and do not represent a material interest rate risk to us. As of July 30, 2011, we had \$8.5 million in long term debt obligations under our Term Loan Agreement entered into during the First Quarter.

Foreign Currency: We conduct business in various parts of the world. We are exposed to fluctuations in exchange rates to the extent that the foreign currency exchange rate fluctuates in countries where our licensees do business, and significant fluctuations in exchange rates could result in a material affect on our results of operations or cash flow. For Fiscal 2011, revenues from international licensing comprised 46.7% of our consolidated revenues. For the Six Months, international licensing royalties comprised 39.2% of our total revenues. A hypothetical 10% strengthening of the U.S. dollar relative to the foreign currencies of countries where we operate would have negatively affected the Six Months revenues by approximately \$0.5 million, which represents 3.9% of the total revenues reported for the Six Months.

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Most of our international licensees are required to pay the royalty revenues owed to us in U.S. dollars. As a consequence, the past weakening of the U.S. dollar has benefited us in that the total royalty revenues reported from our international licensees increases when the dollar weakens against such foreign currencies. Conversely, any strengthening of the U.S. dollar has not benefited us. In the future, should the dollar strengthen against such foreign currencies, the total royalty revenues reported by us from such licensees would reflect such changes in the currency exchange rates. Accordingly, a strengthening dollar, compared to current exchange rates, would likely result in lower reported royalty revenues than otherwise would be reported as a result of such unfavorable exchange rate movements.

ITEM 4. CONTROLS AND PROCEDURES

(a) *Evaluation of disclosure controls and procedures.* Cherokee maintains disclosure controls and procedures, as such term is defined under Exchange Act Rule 13a-15 (e) that are designed to ensure that information required to be disclosed in Cherokee's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to Cherokee's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Cherokee has carried out an evaluation under the supervision and with the participation of Cherokee's management, including Cherokee's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Cherokee's disclosure controls and procedures. Based upon their evaluation and subject to the foregoing, the Chief Executive Officer and Chief Financial Officer concluded that Cherokee's disclosure controls and procedures were effective as of July 30, 2011.

(b) *Changes in internal controls.* Management determined that as of July 30, 2011, there have been no changes in Cherokee's internal controls over financial reporting that occurred during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the ordinary course of business, from time to time we become involved in legal claims and litigation. In the opinion of management, based on consultations with legal counsel, the disposition of litigation currently pending against us is unlikely to have, individually or in the aggregate, a materially adverse effect on our business, financial position or results of operations.

ITEM 1A. RISK FACTORS

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In addition to the other information contained herein or incorporated herein by reference, the risks and uncertainties and other factors described below could have a material adverse effect on our business, financial condition, results of operations and share price and could also cause our future business, financial condition and results of operations to differ materially from the results contemplated by any forward-looking statement we may make herein, in any other document we file with the Securities and Exchange Commission, or in any press release or other written or oral statement we may make. Please also see Item 2. Management's Discussion and Analysis of Financial Condition And Results of Operations Cautionary Note Regarding Forward-Looking Statements for additional risks and uncertainties applicable to us.

Our business is subject to intense competition.

Royalties paid to us under our licensing agreements are generally based on a percentage of our licensee's net sales of licensed products. Cherokee, Carole Little and Sideout brand footwear, apparel, and accessories, which are manufactured and sold by both domestic and international wholesalers and retail licensees, are subject to extensive competition by numerous domestic and foreign companies. Such competitors with respect to the Cherokee brand include Polo Ralph Lauren, Tommy Hilfiger, Liz Claiborne, and private label brands such as Faded Glory, Arizona, and Route 66, developed by retailers. Competitors with respect to the Sideout brand include Quiksilver, Nike and other active wear companies. Factors which shape the competitive environment include quality of garment construction and design, brand name, style and color selection, price and the manufacturer's ability to respond quickly to the retailer on a national basis. In recognition of the increasing trend towards consolidation of retailers and greater emphasis by retailers on the manufacture of private label merchandise, in the United States our business plan focuses on creating strategic alliances with major retailers for their sale of products bearing our brands through the licensing of our trademarks directly to retailers. Therefore, our degree of success is dependent on the strength of our brands, consumer acceptance of and desire for our brands, our licensees' ability to design, manufacture and sell products bearing our brands and to respond to ever-changing consumer demands, and any significant failure by our licensees to do so could have a material adverse effect on our business prospects, financial condition, results of operations and liquidity. We cannot control the level of resources that our licensees commit to supporting our brands, and our licensees may choose to support other brands to the detriment of ours.

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There are numerous risk factors that apply to the businesses of retailers that can affect their level of sales of products that carry our brands. Any decline in sales by our licensees can adversely affect our revenues. Factors that may adversely affect retailers include the following: weather; changes in the availability or cost of capital; shifts in the seasonality of shopping patterns; labor strikes or other work interruptions including work interruptions that impact supply chains and transport vendors; the impact of excess retail capacity; changes in the cost of accepting various payment methods and changes in the rate of utilization of these payment methods; material acquisitions or dispositions; investments in new business strategies; the success or failure of significant new business ventures or technologies; actions taken or omitted to be taken by legislative, regulatory, judicial and other governmental authorities and officials; and natural disasters, the outbreak of war, acts of terrorism or other significant national or international events.

In addition, other companies owning established trademarks could also enter into similar arrangements with retailers, including our existing retail partners, competing for limited floor pad and rack space.

Our business is largely dependent on royalties from two licensees, Target and Tesco, which accounted for 42.1% and 27.1%, respectively, of our consolidated licensing revenues in Fiscal 2011, and accounted for 48.4% and 15.6%, respectively, of our Six Months licensing revenues.

During Fiscal 2011, 42.1% of our licensing revenues were generated from Target and 27.1% of our licensing revenues were generated from Tesco. For the Six Months, 48.4% and 15.6%, respectively, of our licensing revenues were generated from Target and Tesco. We could suffer substantially decreased royalty revenues and cash flow under the Restated Target Agreement if Target were to reduce its sales of Cherokee branded products while continuing to pay the minimum royalties of \$9.0 million per fiscal year required under such agreement. We are unsure whether we would be able to replace the royalty payments received from Target and Tesco. The termination of either of these license agreements would have a material adverse effect upon our revenues and cash flow. Together, these two licensees accounted for 69.2% of our consolidated licensing revenues in Fiscal 2011 and accounted for 64.0% of our consolidated licensing revenues in our Six Months.

Our business may be negatively impacted by general economic conditions and the current global financial crisis.

Our performance is subject to worldwide economic conditions and its corresponding impact on the levels of consumer spending which may affect our licensees' sales. Consumer spending is showing signs of stabilization; however it is difficult to predict future levels of consumer spending and any such predictions are inherently uncertain. The worldwide apparel industry is heavily influenced by general economic cycles. Purchases of apparel and accessories tend to decline in periods of recession or uncertainty regarding future economic prospects, as disposable income typically declines. Many factors affect the level of consumer spending in the apparel industries, including, among others, prevailing economic conditions, levels of employment, salaries and wage rates, energy costs, interest rates, the availability of consumer credit, taxation and consumer confidence in future economic conditions. During periods of economic uncertainty, we may not be able to maintain, or increase our revenues. As a result, our operating results may be materially affected by trends in the United States or global economy.

The risks associated with our business are more acute during periods of economic slowdown or recession. In addition to other consequences, these periods may be accompanied by decreased consumer spending generally, as well as decreased demand for, or additional downward pricing pressure on, the products carrying our brands.

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Accordingly, any prolonged economic slowdown or a lengthy or severe recession with respect to either the U.S. or the global economy is likely to have a material adverse effect on our results of operations, financial condition and business prospects.

Our business and the success of our products could be harmed if we are unable to maintain the strength of our brands.

Our success to date has been due in large part to the strength of our brands. If we are unable to timely and appropriately respond to changing consumer demand, the strength of our brands may be impaired. Even if we react appropriately to changes in consumer preferences, consumers may consider one or more of our brands to be outdated or associate one or more of our brands with styles that are no longer popular. In the past, many apparel companies have experienced periods of rapid growth in sales and earnings followed by periods of declining sales and losses. Our business may be similarly affected in the future.

We are dependent on our intellectual property, and we cannot assure you that we will be able to successfully protect our rights.

We hold various trademarks including Cherokee, Sideout, Carole Little and others in connection with apparel, footwear, home and accessories. These trademarks are vital to the success and future growth of our business. These trademarks are registered with the United States Patent and Trademark Office and in numerous other countries. We also hold several trademark applications for Cherokee and Sideout in other countries. There can be no assurance that the actions taken by us to establish and protect our trademarks and other proprietary rights will prevent imitation of our products or infringement of our intellectual property rights by others, or prevent the loss of licensing revenue or other damages caused thereby. In addition, the laws of several countries in which we have licensed our intellectual property may not protect our intellectual property rights to the same extent as the laws of the United States. Despite our efforts to protect our intellectual property rights, unauthorized parties may attempt to copy aspects of our intellectual property, which could have a material adverse effect on our business prospects, financial condition, results of operations and liquidity. In the future we may be required to assert infringement claims against third parties, and there can be no assurance that one or more parties will not assert infringement claims against us. Any resulting litigation could result in significant expense and divert the efforts of our management personnel whether or not such litigation is determined in our favor.

We must successfully maintain and/or upgrade our information technology systems.

We rely on various information technology systems, including our newly purchased enterprise resource planning (ERP) system that was fully implemented during the First Quarter, to manage our operations, which subjects us to inherent costs and risks associated with maintaining, upgrading, replacing and changing these systems, including impairment of our information technology, potential disruption of our internal control systems, substantial capital expenditures, demands on management time and other risks of delays or difficulties in upgrading, transitioning to new systems or of integrating new systems into our current systems.

We are dependent on our key management personnel and we recently appointed a new Chief Executive Officer and a new Chief Financial Officer.

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Our success is highly dependent upon the continued services of our key executives, including, Henry Stupp, our Chief Executive Officer, Howard Siegel, our President and Chief Operating Officer and Mark DiSiena, our Chief Financial Officer. We have a limited number of employees and Mr. Stupp's and our other executives' leadership and experience in the apparel licensing industry is important to the successful implementation of our business and marketing strategy. We do not carry key person life insurance covering any of our executives. The loss of the services of Mr. Stupp or our other key executives could have a material adverse effect on our business prospects, financial condition, results of operations and liquidity. In addition, on August 26, 2010, we experienced a transition in our executive management team, in connection with the appointment of Henry Stupp as our Chief Executive Officer and the appointment of our former Chief Executive Officer, Robert Margolis, as our Executive Chairman, who resigned from Cherokee on January 28, 2011. Further, on November 5, 2010 we announced that our former Chief Financial Officer, Russell J. Riopelle, would be leaving Cherokee in mid December. On November 11, 2010, we announced that we hired Mark DiSiena, who replaced Mr. Riopelle as our Chief Financial Officer following Mr. Riopelle's departure from Cherokee on December 17, 2010. Our former Executive Chairman, Robert Margolis, resigned from Cherokee on January 28, 2011. Neither Mr. Stupp nor Mr. DiSiena has worked with

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our existing executive management team prior to their joining us last year. We cannot assure you that either of these management transitions will not result in some disruption of our business. If either our new Chief Executive Officer or our new Chief Financial Officer is unable to work with our existing management team to implement our strategies, manage our operations and accomplish our objectives, our business, operations and financial results could be impaired.

In February 2011 we consummated a debt financing of \$10,000,000 in principal in order to enable us to meet our payment obligations to our former Executive Chairman.

In connection with the resignation of our former Executive Chairman, Robert Margolis, on January 28, 2011, we entered into a Separation Agreement and General Release of all Claims (the "Separation Agreement"), with Mr. Margolis. Pursuant to the Separation Agreement, (i) on February 17, 2011, we paid Mr. Margolis a one-time lump sum payment equal to \$2,260,000 and (ii) on April 1, 2011, we paid Mr. Margolis his final annual performance bonus for Fiscal 2011 of \$1.8 million. In addition, pursuant to the Separation Agreement, on February 7, 2011, we repurchased 400,000 shares (the "Repurchase Shares") of our Common Stock for aggregate proceeds of \$7,260,000. As payment for the Repurchase Shares, we issued promissory notes to affiliates of Mr. Margolis in the principal amount of \$7,260,000 (collectively, the "Margolis Notes"). The Margolis Notes bore interest at an annual rate of 3% and were repaid by us in full on February 17, 2011.

In order to repay the Margolis Notes and meet our other obligations to Mr. Margolis under the Separation Agreement, on February 16, 2011, we entered into a term loan agreement with U.S. Bank (the "Bank"), as amended on September 6, 2011, pursuant to which we borrowed \$10,000,000 in principal (the "Loan Facility") and which bears interest at a floating rate equal to either (i) the Bank's prime rate minus 0.25% or (ii) 2.75% plus the 1, 2 or 3 month LIBOR rate, as selected by Cherokee pursuant to the terms of the Loan Facility. The Loan Facility is to be repaid in equal monthly installments of \$277,778 over the next three years following the date of the loan. The Loan Facility is secured by all of Cherokee's assets and guaranteed by Cherokee's wholly owned subsidiary, Spell C. LLC.

We may not pay dividends regularly or at all in the future.

Although we have paid dividends during each quarter since December 2003, and including during the first and second quarters of Fiscal 2012, our Board of Directors may reduce or discontinue dividends at any time for any reason it deems relevant and there can be no assurances that we will continue to generate excess cash to pay dividends, or that we will continue to pay dividends with such excess cash if other, more compelling business opportunities are available, as determined by our Board of Directors. Our ability to generate excess cash from our operations in the future is dependent upon a variety of factors, including Cherokee's financial condition, results of operations, cash flow, capital requirements and other factors. In Fiscal 2011, we paid a total of \$13.5 million in dividends, which was materially greater than our net income of \$7.7 million for Fiscal 2011. In recognition of the fact that our payment of dividends could not continue at historical levels beyond Fiscal 2011 unless cash flow from operations increases substantially, on January 31, 2011, we announced that we further reduced our future quarterly dividend payments from \$0.38 per share to \$0.20 per share, which more closely aligned our dividend payments with our expected cash flow from operations while allowing us to retain a portion of our cash flow to satisfy our debt obligations and to invest in our business. Should our future dividend payments exceed our cash from operations, we will reduce the excess cash on our balance sheet and our Board of Directors may elect to further reduce or eliminate future dividend payments. Furthermore, should the dividend tax laws change such that taxes on dividends become higher than they currently are, we may further reduce or eliminate the dividends we pay to our stockholders in favor of other ways to increase value for our stockholders.

The trading price of our stock may be volatile.

The trading price of our common stock is likely to be subject to fluctuations as a result of various factors impacting our business, including (i) our financial results, (ii) announcements by us, our retail partners or by our competitors, as applicable, regarding or affecting the retail environment either domestically or internationally, our existing license agreements, our existing brand representations, new license agreements, new brand representations or strategic alliances or other agreements, (iii) recruitment or departure of key personnel, (iv) changes in the estimates of our financial results or changes in the recommendations of any securities

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analysts that elect to follow our common stock, and (v) market conditions in the retail industry and the economy as a whole.

Our Certificate of Incorporation allows our Board of Directors to issue up to 1,000,000 shares of blank check preferred stock.

Our Certificate of Incorporation allows our Board of Directors to issue up to 1,000,000 shares of blank check preferred stock, without action by our stockholders. Such shares of preferred stock may be issued on terms determined by our Board of Directors, and may have rights, privileges and preferences superior to those of our common stock. Without limiting the foregoing, (i) such shares of preferred stock could have liquidation rights that are senior to the liquidation preference applicable to our common stock, (ii) such shares of preferred stock could have voting or conversion rights, which could adversely affect the voting power of the holders of our common stock and (iii) the ownership interest of holders of our common stock will be diluted following the issuance of any such shares of preferred stock.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Pursuant to our employment agreement with Henry Stupp, as amended (the Employment Agreement), on July 28, 2011, Mr. Stupp purchased 12,562 shares of Cherokee's common stock (the July 2011 Shares) at a per share price of \$15.92 (which was equal to the closing price of Cherokee's common stock on such date), for aggregate proceeds of approximately \$200,000. Mr. Stupp previously purchased 81,967 shares of Cherokee's Common Stock (the Initial Shares) for investment proceeds of \$1,500,000 on August 26, 2010 pursuant to the Employment Agreement. Pursuant to the Employment Agreement, Mr. Stupp has agreed to purchase, and Cherokee has agreed to sell, an additional \$600,000 in Cherokee's Common Stock, in three installments of \$200,000 to occur on or before October 31, 2011, January 31, 2012 and April 30, 2012. The amount of shares to be purchased by Mr. Stupp in such transactions are to equal that number of shares of Cherokee's common stock equal to \$200,000, divided by the closing sale price of Cherokee's common stock on the date of such purchase and sale (the Subsequent Shares and, together with the Initial Shares and the July 2011 Shares, the Shares). Mr. Stupp has agreed to certain lock up restrictions regarding his ability to resell or otherwise dispose of any of the Shares as set forth in the Employment Agreement. Pursuant to the Employment Agreement, Cherokee has agreed to file with the SEC a registration statement, or registration statements if necessary, on an appropriate form(s) to effect the registration for resale of both the Shares and the shares of Common Stock that may be acquired upon exercise of the option granted to Mr. Stupp pursuant to the Employment Agreement. The Company intends to use the proceeds from the sales of the Shares to Mr. Stupp as working capital.

Issuer Repurchases of Common Stock

On July 22, 1999, our Board of Directors authorized the repurchase of up to one million shares of our then outstanding common stock. Pursuant to this directive, and including certain repurchases of our common stock that were effected during Fiscal 2009 and during the Second Quarter as are described below, as of July 30, 2011 we have used cash of \$7.9 million to repurchase and retire a total of 741,516 shares of our common stock since the stock repurchases were authorized (excluding our one-time repurchase of 400,000 shares of our common stock held by affiliates of our former Executive Chairman, discussed below and in our Annual Report on Form 10-K for Fiscal 2011). Our Board of Directors subsequently authorized and approved the extension of the expiration date of our stock repurchase program to January 31, 2012 and increased the number of remaining shares which could currently be repurchased from time to time in the open market at prevailing market prices or in privately negotiated transactions to a total of 800,000 shares of our common stock.

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During the second quarter of Fiscal 2009, we purchased and retired 10,155 shares of our common stock at an average price of \$21.59. During the third quarter of Fiscal 2009, we repurchased and retired 99,561 shares of our common stock at an average price of \$17.62. We did not repurchase any shares in the fourth quarter of Fiscal 2009. During Fiscal 2010 and Fiscal 2011, we did not repurchase any shares of our common stock.

On January 28, 2011, we entered into a separation agreement with our former Executive Chairman, Robert Margolis, pursuant to which we irrevocably committed to repurchase 400,000 shares of our common stock from Mr. Margolis or his affiliates at a price of \$18.15 per share, or \$7.26 million in total. The repurchase was consummated on February 7, 2011. On February 17, 2011, we retired the 400,000 repurchased shares.

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During the First Quarter we did not repurchase any shares of our common stock. During the Second Quarter, we purchased and retired 24,000 shares of our common stock at an average price of \$16.47.

Continued repurchases of our stock, if any, will be made from time to time in the open market at prevailing market prices or in privately negotiated transactions.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number Shares that May Yet Be Purchased Under the Plans or Programs
May 1, 2011 – May 31, 2011				690,284
June 1, 2011 – June 30, 2011				690,284
July 1, 2011 – July 30, 2011	24,000	\$ 16.47	24,000	666,284
Total	24,000		24,000	666,284

ITEM 4. (REMOVED AND RESERVED)**ITEM 5. OTHER INFORMATION***Amendment and Restatement of Bylaws*

As previously reported in our Current Report on Form 8-K, which was filed with the Commission on June 28, 2011, on June 22, 2011, our Board of Directors adopted Amended and Restated Bylaws (the "Restated Bylaws"). The amendment and restatement of the Bylaws, which is effective as of June 22, 2011, includes provisions regarding communication and disclosure by stockholders to the Company in connection with the Company's annual meeting, as well as enhanced procedural and forum mechanics and other provisions intended to reflect changes in law and practice in recent years. Pursuant to the Restated Bylaws, and as set forth in Section 2.11 thereof, a stockholder wishing to nominate a director for service on our Board of Directors must provide timely notice in writing to Cherokee's Secretary. To be timely, in the case of a stockholder seeking to have a nomination included in our proxy statement or information statement, a stockholder's notice must be delivered to or mailed and received at our principal executive offices not less than 120 days or more than 180 days prior to the first anniversary of the date on which we first mailed our proxy materials for the previous year's annual meeting of stockholders. However, if we did not hold an annual meeting the previous year, or if the date of our annual meeting is advanced more than 30 days prior to or delayed by more than 30 days after the anniversary of the preceding year's annual meeting, then to be timely, notice by the stockholder must be delivered to the Secretary at our principal executive offices not later than the close of business on the later of (i) the 90th day prior to such annual meeting or (ii) the 15th day following the day on which public announcement of the date of such meeting is first made. If the stockholder is not seeking inclusion of the nomination in our proxy statement or information statement, timely notice consists of a stockholder's notice delivered to or mailed and received at our principal executive offices not less than 90 days prior to the date of the annual meeting.

Table of Contents*Amendment to Loan Agreement*

On February 16, 2011, Cherokee and U.S. Bank National Association (the *Bank*) entered into a Term Loan Agreement (the *Loan Agreement*). Pursuant to the Loan Agreement, Cherokee borrowed \$10,000,000 in principal from the Bank (the *Loan*). The Loan is to be repaid in equal monthly installments of \$277,778 plus interest over three years, with the balance due at maturity, and with interest on the Loan calculated at a floating rate equal to either (i) the Bank's prime rate minus 0.25% or (ii) 2.75% plus the 1, 2 or 3 month LIBOR rate, as selected by Cherokee. The Loan Agreement contains various affirmative and negative covenants that are customary for loan agreements and transactions of this type, including limitations on our ability to incur debt or other liabilities and limitations on our ability to consummate acquisitions in any fiscal year in excess of \$3,000,000 or in excess of \$6,000,000 in the aggregate while the Loan is outstanding. Further, as collateral for the Loan, the Company granted a security interest in favor of the Bank in all of Cherokee's assets, and the Loan is guaranteed by Cherokee's wholly owned subsidiary, Spell C. LLC. Proceeds from the Loan were primarily used to satisfy the Company's promissory note payable to our former Executive Chairman. On September 6, 2011, we entered into an amendment to the Loan Agreement to (i) modify the covenants relating to, and related definitions of, the *fixed charge coverage ratio* and *tangible net worth* as such terms are defined in the Amendment, and (ii) modify the covenant relating to the Company's ability to make certain permitted acquisitions under the Loan Agreement, such that the Company is now permitted, subject to certain conditions, to consummate acquisitions in any fiscal year in amounts below \$5,000,000 or in amounts below \$10,000,000 in the aggregate while the Loan is outstanding.

ITEM 6. EXHIBITS**(a) Exhibits**

Exhibit Number	Description of Exhibit
3.2	Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 of Cherokee's Current Report on Form 8-K, filed with the Commission on June 28, 2011).
10.1	Third Amendment to Employment Agreement, by and between Cherokee Inc. and Henry Stupp, dated as of July 28, 2011 (incorporated by reference to Exhibit 10.1 of Cherokee's Current Report on Form 8-K filed with the Commission on August 2, 2011).
10.2*	First Amendment to Term Loan Agreement, by and between Cherokee and U.S. Bank National Association, dated as of September 6, 2011.
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	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.
32.2*	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.
101	The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended July 30, 2011, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets at January 29, 2011 and July 30, 2011; (ii) Consolidated Statement of Operations for the three months and six months ended July 31, 2010 and July 30, 2011; (iii) Condensed Consolidated Statement of Stockholders' Equity for the six months ended July 30, 2011; (iv) Consolidated Statements of Cash Flows for the six months ended July 31, 2010 and July 30, 2011; and (v) Notes to Condensed Consolidated Financial Statements, tagged as block of text.

* Filed herewith.

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Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

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SIGNATURES

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

Dated: September 8, 2011

CHEROKEE INC.

By:

/s/ Henry Stupp

Henry Stupp
Chief Executive Officer
(Principal Executive Officer)

By:

/s/ Mark DiSiena

Mark DiSiena
Chief Financial Officer
(Principal Financial Officer and Principal Accounting
Officer)