LANDS' END, INC.
Form 10-Q
December 01, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
x Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended October 28, 2016
-OR-
¨ Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from to to .
Commission File Number: 001-09769

Lands' End, Inc.
(Exact name of registrant as specified in its charter)

Delaware	36-2512786
(State or Other Jurisdiction of Incorporation of Organization)	(I.R.S. Employer Identification No.)
1 Lands' End Lane Dodgeville, Wisconsin	53595
(Address of Principal Executive Offices)	(Zip Code)

Issuer's Telephone Number, Including Area Code: (608) 935-9341

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 x 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 x NO ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨ Accelerated filer x

Non-accelerated filer ¨ Smaller Reporting Company ¨

Indicate by check mark whether the Registrant is a shell company. YES ¨ NO x

As of December 1, 2016, the registrant had 32,029,359 shares of common stock, $0.01 par value, outstanding.

LANDS’ END, INC.
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FOR THE PERIOD ENDED OCTOBER 28, 2016
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ITEM 1. FINANCIAL STATEMENTS
LANDS' END, INC.
Condensed Consolidated Statements of Operations
(Unaudited)

(in thousands except per share data)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Net revenue	$311,476	$334,434	$876,919	$946,235
Cost of sales (excluding depreciation and amortization)	177,825	172,019	477,446	492,756
Gross profit	133,651	162,415	399,473	453,479
Selling and administrative	132,365	135,867	390,291	394,261
Depreciation and amortization	4,795	4,260	13,419	12,874
Other operating (income), net	(86)	(1,009)	(40)	(3,366)
Operating (loss) income	(3,423)	23,297	(4,197)	49,710
Interest expense	6,149	6,204	18,493	18,615
Other (income) expense, net	(432)	796	(1,413)	(210)
(Loss) income before income taxes	(9,140)	16,297	(21,277)	31,305
Income tax (benefit) expense	(1,918)	5,572	(6,316)	11,395
NET (LOSS) INCOME	$(7,222)	$10,725	$(14,961)	$19,910
NET (LOSS) INCOME PER COMMON SHARE (Note 2)				
Basic:	$(0.23)	$0.34	$(0.47)	$0.62
Diluted:	$(0.23)	$0.33	$(0.47)	$0.62
Basic weighted average common shares outstanding	32,029	31,991	32,018	31,975
Diluted weighted average common shares outstanding	32,029	32,059	32,018	32,042

See accompanying Notes to Condensed Consolidated Financial Statements.

LANDS’ END, INC.
Condensed Consolidated Statements of Comprehensive Operations
(Unaudited)

(in thousands)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
NET (LOSS) INCOME	$(7,222)	$10,725	$(14,961)	$19,910
Other comprehensive (loss) income, net of tax				
Foreign currency translation adjustments	(2,183)	260	(2,952)	925
COMPREHENSIVE (LOSS) INCOME	$(9,405)	$10,985	$(17,913)	$20,835

See accompanying Notes to Condensed Consolidated Financial Statements.

LANDS' END, INC.
Condensed Consolidated Balance Sheets

(in thousands, except share data)	October 28, 2016 (unaudited)	October 30, 2015 (unaudited)	January 29, 2016
ASSETS			
Current assets			
Cash and cash equivalents	$131,532	$104,986	$228,368
Restricted cash	3,300	3,300	3,300
Accounts receivable, net	40,101	37,875	32,061
Inventories, net	425,290	436,712	329,203
Prepaid expenses and other current assets	40,942	40,833	23,618
Total current assets	641,165	623,706	616,550
Property and equipment, net	115,871	105,661	109,831
Goodwill	110,000	110,000	110,000
Intangible asset, net	430,000	528,300	430,000
Other assets	16,142	14,352	15,145
TOTAL ASSETS	$1,313,178	$1,382,019	$1,281,526
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities			
Accounts payable	$180,608	$151,429	$146,097
Other current liabilities	101,093	107,596	83,992
Total current liabilities	281,701	259,025	230,089
Long-term debt, net	490,992	494,788	493,838
Long-term deferred tax liabilities	158,048	184,926	157,252
Other liabilities	16,766	16,390	15,838
TOTAL LIABILITIES	947,507	955,129	897,017
Commitments and contingencies			
STOCKHOLDERS' EQUITY			
Common stock, par value $0.01- authorized: 480,000,000 shares; issued and outstanding: 32,029,359, 31,991,343 and 31,991,668, respectively	320	320	320
Additional paid-in capital	343,319	344,156	344,244
Retained earnings	34,368	88,787	49,329
Accumulated other comprehensive loss	(12,336)	(6,373)	(9,384)
Total stockholders' equity	365,671	426,890	384,509
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$1,313,178	$1,382,019	$1,281,526

See accompanying Notes to Condensed Consolidated Financial Statements.
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LANDS' END, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

(in thousands)	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (loss) income	$(14,961)	$19,910
Adjustments to reconcile net (loss) income to net cash used in operating activities:		
Depreciation and amortization	13,419	12,874
Product recall	(212)	(3,371)
Amortization of debt issuance costs	1,284	1,313
Loss on disposal of property and equipment	172	5
Stock-based compensation	1,578	2,307
Deferred income taxes	839	3,381
Change in operating assets and liabilities:		
Inventories	(99,997)	(134,690)
Accounts payable	40,186	20,078
Other operating assets	(25,100)	(18,124)
Other operating liabilities	15,537	1,523
Net cash used in operating activities	(67,255)	(94,794)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of property and equipment	44	—
Purchases of property and equipment	(26,083)	(18,117)
Net cash used in investing activities	(26,039)	(18,117)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on term loan facility	(3,863)	(3,863)
Net cash used in financing activities	(3,863)	(3,863)
Effects of exchange rate changes on cash	321	306
NET DECREASE IN CASH AND CASH EQUIVALENTS	(96,836)	(116,468)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	228,368	221,454
CASH AND CASH EQUIVALENTS, END OF PERIOD	$131,532	$104,986
SUPPLEMENTAL CASH FLOW DATA		
Unpaid liability to acquire property and equipment	$3,101	$2,695
Income taxes paid, net of refund	$3,220	$19,714
Interest paid	$16,892	$17,037

See accompanying Notes to Condensed Consolidated Financial Statements.

LANDS’ END, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
NOTE 1. BACKGROUND AND BASIS OF PRESENTATION
Description of Business and Separation

Lands' End, Inc. (“Lands’ End” or the “Company”) is a leading multi-channel retailer of clothing, accessories and footwear, as well as home products. Lands' End offers products through catalogs, online at www.landsend.com, www.canvasbylandsend.com and affiliated specialty and international websites, and through retail locations, primarily at Lands’ End Shops at Sears, stand-alone Lands’ End Inlet stores and international shop-in-shops that sell merchandise in various retail department stores.

Terms that are commonly used in the Company's notes to condensed consolidated financial statements are defined as follows:

- ABL Facility - Asset-based senior secured credit agreements, dated as of April 4, 2014, with Bank of America, N.A and certain other lenders
- ASC - Financial Accounting Standards Board Accounting Standards Codification, which serves as the source for authoritative GAAP, except that rules and interpretive releases by the SEC are also sources of authoritative GAAP for Securities and Exchange Commission registrants
- ASU - FASB Accounting Standards Update
- CAM - Common area maintenance for leased properties
- Debt Facilities - Collectively, the ABL Facility and the Term Loan Facility
- EPS - (Loss) earnings per share
- ESL - ESL Investments, Inc. and its investment affiliates, including Edward S. Lampert
- FASB - Financial Accounting Standards Board
- First Quarter 2016 - The thirteen weeks ended April 29, 2016
- Fiscal 2016 - The fifty-two weeks ending January 27, 2017
- Fiscal 2015 - The fifty-two weeks ended January 29, 2016
- Fiscal November 2016 - the four week fiscal month ending November 25, 2016
- GAAP - Accounting principles generally accepted in the United States
- LIBOR - London inter-bank offered rate
- Sears Holdings or Sears Holdings Corporation - Sears Holdings Corporation, a Delaware Corporation, and its consolidated subsidiaries (other than, for all periods following the Separation, Lands' End)
- SEC - United States Securities and Exchange Commission
- Second Quarter 2016 - The thirteen weeks ended July 29, 2016
- Separation - On April 4, 2014 Sears Holdings distributed 100% of the outstanding common stock of Lands' End to its shareholders
- SYW or Shop Your Way - Shop Your Way member loyalty program
- Tax Sharing Agreement - A tax sharing agreement entered into by Sears Holdings Corporation and Lands' End in connection with the Separation

• Term Loan Facility - Term loan credit agreements, dated as of April 4, 2014, with Bank of America, N.A. and certain other lenders
• Third Quarter 2016 - The thirteen weeks ended October 28, 2016
• Third Quarter 2015 - The thirteen weeks ended October 30, 2015
• UTBs - Gross unrecognized tax benefits related to uncertain tax positions
• Year to Date 2016 - the thirty-nine weeks ended October 28, 2016
• Year to Date 2015 - the thirty-nine weeks ended October 30, 2015

Basis of Presentation

The Condensed Consolidated Financial Statements include the accounts of Lands' End, Inc. and its subsidiaries. All intercompany transactions and balances have been eliminated.

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with GAAP for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all material adjustments which are of a normal and recurring nature necessary for a fair presentation of the results for the periods presented have been reflected. Dollar amounts are reported in thousands, except per share data, unless otherwise noted. Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with information included in the Lands' End Annual Report on Form 10-K filed with the SEC on April 1, 2016.

Reclassifications

In April 2015, FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which changes the required presentation of debt issuance costs from an asset on the balance sheet to a deduction from related debt liability, and which was adopted by the Company in the First Quarter 2016. The reclassifications resulting from the adoption of this ASU relate to Prepaid expenses and other current assets and Other assets as of January 29, 2016 and October 30, 2015 that were reclassified to Long-term debt. This reclassification reduced our current and total assets and our total liabilities, as previously reported in the Condensed Consolidated Balance Sheet for January 29, 2016 and October 30, 2015. This reclassification had no effect on the Condensed Consolidated Statements of Operations, Comprehensive Operations, Stockholders’ Equity or Cash Flows as previously reported. See Note 4, Debt, for further discussion.

NOTE 2. (LOSS) EARNINGS PER SHARE

The numerator for both basic and diluted EPS is net (loss) income. The denominator for basic EPS is based upon the number of weighted average shares of Lands’ End common stock outstanding during the reporting periods. The denominator for diluted EPS is based upon the number of weighted average shares of Lands' End common stock and common stock equivalents outstanding during the reporting periods using the treasury stock method in accordance with the ASC.

The following table summarizes the components of basic and diluted EPS:

(in thousands, except per share amounts)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Net (loss) income	$(7,222)	$ 10,725	$(14,961)	$ 19,910
Basic weighted average shares outstanding	32,029	31,991	32,018	31,975
Dilutive effect of stock awards	—	68	—	67
Diluted weighted average shares outstanding	32,029	32,059	32,018	32,042
Basic (loss) earnings per share	$(0.23)	$ 0.34	$(0.47)	$ 0.62
Diluted (loss) earnings per share	$(0.23)	$ 0.33	$(0.47)	$ 0.62

Anti-dilutive stock awards are comprised of awards which are anti-dilutive in the application of the treasury stock method and are excluded from the diluted weighted average shares outstanding. Total anti-dilutive stock awards were 17,719 and 30,673 shares for the Third Quarter 2016 and Year to Date 2016, respectively, due to the net loss reported. Total anti-dilutive stock awards were 129 and 126,602 shares for the Third Quarter 2015 and Year to Date 2015, respectively.

NOTE 3. OTHER COMPREHENSIVE (LOSS)

Other comprehensive (loss) income encompasses all changes in equity other than those arising from transactions with stockholders, and is comprised solely of foreign currency translation adjustments.

(in thousands)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Beginning balance: Accumulated other comprehensive loss (net of tax of $5,467, $3,572, $5,053 and $3,931, respectively)	$(10,153)	$ (6,633)	$(9,384)	$ (7,298)
Other comprehensive (loss) income:				
Foreign currency translation adjustments (net of tax (benefit) expense of $1,176, $(141), $1,590 and $(500), respectively)	(2,183)	260	(2,952)	925
Ending balance: Accumulated other comprehensive loss (net of tax of $6,643, $3,431, $6,643 and $3,431, respectively)	$(12,336)	$ (6,373)	$(12,336)	$ (6,373)

No amounts were reclassified out of Accumulated other comprehensive loss during any of the periods presented.

NOTE 4. DEBT

The Company's debt consisted of the following:

	October 28, 2016		October 30, 2015		January 29, 2016	
	Amount	Rate	Amount	Rate	Amount	Rate
Term Loan Facility, maturing April 4, 2021	$502,125	4.25%	$507,275	4.25%	$505,988	4.25%
ABL Facility, maturing April 4, 2019	—	— %	—	— %	—	— %
	502,125		507,275		505,988	
Less: Current maturities in Other current liabilities, net	5,150		5,150		5,150	
Less: Unamortized debt issuance costs	5,983		7,337		7,000	
Long-term debt, net	$490,992		$494,788		$493,838	

The following table summarizes the Company's borrowing availability under the ABL Facility:

	October 28, 2016	October 30, 2015	January 29, 2016
ABL maximum borrowing	$175,000	$175,000	$175,000
Outstanding Letters of Credit	13,845	18,523	24,311
Borrowing availability under ABL	$161,155	$156,477	$150,689

During First Quarter 2016, the Company adopted ASU 2015-03, Simplifying the Presentation of Debt Issuance, which requires an entity to present debt issuance costs as a deduction from the related debt liability. To conform to the current year presentation the Company reclassified $1.4 million of Prepaid expenses and other current assets and $6.0 million of Other assets to Long-term debt as of October 30, 2015. Similarly, as of January 29, 2016, the company reclassified $1.4 million of Prepaid expenses and other current assets and $5.6 million of Other assets to Long-term debt.

Interest; Fees

The interest rates per annum applicable to the loans under the Debt Facilities are based on a fluctuating rate of interest measured by reference to, at the borrowers' election, either (i) an adjusted LIBOR rate plus a borrowing margin, or (ii) an alternative base rate plus a borrowing margin. The borrowing margin is fixed for the Term Loan Facility at 3.25% in the case of LIBOR loans and 2.25% in the case of base rate loans. For the Term Loan Facility, LIBOR is subject to a 1% interest rate floor. The borrowing margin for the ABL Facility is subject to adjustment based on the average excess availability under the ABL Facility for the preceding fiscal quarter, and will range from 1.50% to 2.00% in the case of LIBOR borrowings and will range from 0.50% to 1.00% in the case of base rate borrowings.

Customary agency fees are payable in respect of both Debt Facilities. The ABL Facility fees also include (i) commitment fees, based on a percentage ranging from approximately 0.25% to 0.375% of the daily unused portions of the ABL Facility, and (ii) customary letter of credit fees.

Representations and Warranties; Covenants

Subject to specified exceptions, the Debt Facilities contain various representations and warranties and restrictive covenants that, among other things, restrict the ability of Lands' End and its subsidiaries to incur indebtedness (including guarantees), grant liens, make investments, make dividends or distributions with respect to capital stock, make prepayments on other indebtedness, engage in mergers or change the nature of their business. In addition, if excess availability under the ABL Facility falls below the greater of 10% of the loan cap amount or $15.0 million, Lands' End will be required to comply with a minimum fixed charge coverage ratio of 1.0 to 1.0. The Debt Facilities do not otherwise contain financial maintenance covenants. The Company was in compliance with all financial covenants related to the Debt Facilities as of October 28, 2016.

The Debt Facilities contain certain affirmative covenants, including reporting requirements such as delivery of financial statements, certificates and notices of certain events, maintaining insurance, and providing additional guarantees and collateral in certain circumstances.

NOTE 5. STOCK-BASED COMPENSATION

Accounting standards require, among other things, that (i) the fair value of all stock awards be expensed over their respective vesting periods; (ii) the amount of cumulative compensation cost recognized at any date must at least be equal to the portion of the grant-date value of the award that is vested at that date and (iii) compensation expense includes a forfeiture estimate for those shares not expected to vest. Also in accordance with these provisions, for awards that only have a service requirement with multiple vest dates, the Company is required to recognize compensation cost on a straight-line basis over the requisite service period for the entire award.

The Company has granted time vesting stock awards ("Deferred Awards") and performance-based stock awards ("Performance Awards") to employees at management levels and above. Deferred Awards were granted in the form of restricted stock units that only require each recipient to complete a service period. Deferred Awards generally vest over three years or in full after a three year period. Performance Awards were granted in the form of restricted stock units which have, in addition to a service requirement, performance criteria that must be achieved for the awards to be earned. Performance Awards have annual vesting, but due to the performance criteria, are not eligible for straight-line expensing. Therefore, Performance Awards are amortized using a graded expense process. The fair value of all awards is based on the closing price of the Company's common stock on the grant date. Compensation expense is reduced for estimated forfeitures of those awards not expected to vest due to employee turnover.

The following table summarizes the Company's stock-based compensation expense, which is included in Selling and administrative expense in the Condensed Consolidated Statements of Operations:

(in thousands)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Performance Awards	$127	$ 315	$511	$ 1,096
Deferred Awards	(301)	471	1,067	1,211
Total stock-based compensation (benefit) expense	$(174)	$ 786	$1,578	$ 2,307

In Third Quarter 2016 there was a reversal of prior period expense due to the resignation of the former Chief Executive Officer.

Awards Granted Year to Date 2016

The company granted Deferred Awards to various employees during the Year to Date 2016, which generally vest ratably over a three year period. There were no Performance Awards granted in the Year to Date 2016.

Changes in the Company's Unvested Stock Awards Year to Date 2016

Deferred Awards

(in thousands, except per share amounts)	Number of Shares	Weighted Average Grant Date Fair Value
Unvested Deferred Awards, as of January 29, 2016	175	$ 30.87
Granted	225	24.39
Vested	(27)	33.53
Forfeited	(132)	30.25
Unvested Deferred Awards, as of October 28, 2016	241	24.91

Total unrecognized stock-based compensation expense related to unvested Deferred Awards approximated $4.5 million as of October 28, 2016, which will be recognized over a weighted average period of approximately 2.2 years.

Performance Awards

(in thousands, except per share amounts)	Number of Shares	Weighted Average Grant Date Fair Value
Unvested Performance Awards, as of January 29, 2016	109	$ 26.81
Granted	—	—
Vested	(30)	27.84
Forfeited	(10)	26.73
Unvested Performance Awards, as of October 28, 2016	69	26.38

Total unrecognized stock-based compensation expense related to unvested Performance Awards approximated $0.5 million as of October 28, 2016, which will be recognized over a weighted average period of approximately 0.6 years.

NOTE 6. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

The Company determines fair value of financial assets and liabilities based on the following fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1 inputs—unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occurs with sufficient frequency and volume to provide ongoing pricing information.

Level 2 inputs—inputs other than quoted market prices included in Level 1 that are observable, either directly or indirectly, for the asset or liability. Level 2 inputs include, but are not limited to, quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs other than quoted market prices that are observable for the asset or liability, such as interest rate curves and yield curves observable at commonly quoted intervals, volatilities, credit risk and default rates.

Level 3 inputs—unobservable inputs for the asset or liability.

Restricted cash is reflected on the Condensed Consolidated Balance Sheets at fair value. The fair value of restricted cash as of October 28, 2016, October 30, 2015 and January 29, 2016 was $3.3 million based on Level 1 inputs. Restricted cash amounts are valued based upon statements received from financial institutions.

Cash and cash equivalents, accounts receivable, accounts payable and other current liabilities are reflected on the Condensed Consolidated Balance Sheets at cost, which approximates fair value due to the short-term nature of these instruments.

Carrying values and fair values of long-term debt, including the short-term portion, in the Condensed Consolidated Balance Sheets are as follows:

(in thousands)	October 28, 2016		October 30, 2015		January 29, 2016	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt, including short-term portion	$502,125	$386,636	$507,275	$473,668	$505,988	$418,073

Long-term debt was valued utilizing level 2 valuation techniques based on the closing inactive market bid price on October 28, 2016, October 30, 2015, and January 29, 2016. There were no nonfinancial assets or nonfinancial liabilities recognized at fair value on a nonrecurring basis as of October 28, 2016, October 30, 2015, and January 29, 2016.

NOTE 7. GOODWILL AND INTANGIBLE ASSET

The Company's intangible asset, consisting of a trade name, and goodwill were valued as a result of business combinations accounted for under the purchase accounting method. Goodwill represents the excess of the purchase price over the fair value of the net assets acquired. The net carrying amounts of goodwill and trade name are included within the Company's Direct segment.

ASC 350, Intangibles - Goodwill and Other, requires companies to test goodwill and indefinite-lived intangible assets for impairment annually, or more often if an event or circumstance indicates that the carrying amount may not be recoverable. There was no impairment charge recorded for the intangible asset in Year to Date 2016. As a result of the 2015 annual impairment testing the Company recorded a non-cash pretax intangible asset impairment charge of $98.3 million during Fiscal 2015. There was no impairment charge for the intangible asset recorded in any other prior years. There were no impairments of goodwill during any periods presented or since goodwill was first recognized. If actual results are not consistent with our estimates and assumptions used in estimating revenue growth, future cash flows and asset fair values, we could incur further impairment charges for the intangible asset or goodwill, which could have an adverse effect on our results of operations. The annual test for impairment will be conducted as of the end of Fiscal November 2016.

The following summarizes goodwill and the intangible asset:

(in thousands)	October 28, 2016	October 30, 2015	January 29, 2016
Indefinite-lived intangible asset:			
Gross Trade Name	$528,300	$528,300	$528,300
Cumulative impairment	(98,300)	—	(98,300)
Net Trade Name	430,000	528,300	430,000
Total intangible asset, net	$430,000	$528,300	$430,000
Goodwill	$110,000	$110,000	$110,000

NOTE 8. INCOME TAXES

Lands' End and Sears Holdings Corporation entered into a Tax Sharing Agreement in connection with the Separation which governs Sears Holdings Corporation's and Lands' End's respective rights, responsibilities and obligations after the Separation with respect to liabilities for United States federal, state, local and foreign taxes attributable to the Lands' End business. In addition to the allocation of tax liabilities, the Tax Sharing Agreement addresses the preparation and filing of tax returns for such taxes and dispute resolution with taxing authorities regarding such taxes. Generally, Sears Holdings Corporation is liable for all pre-Separation United States federal, state and local income taxes. Lands' End generally is liable for all other income taxes attributable to its business, including all foreign taxes. Prior to the Separation, all tax obligations were settled through Sears Holdings through Net parent company investment. At the date of Separation, certain tax attributes that were recorded in Net parent company investment were reclassified. During the Third Quarter 2016, as a result of filing its Fiscal Year 2015 income tax return, the Company recorded an increase in the deferred tax liabilities and a decrease in Additional paid in capital of $2.1 million related to the calculation of a deferred tax liability related to the LIFO inventory calculation that existed as of the date of the Separation.

As of October 28, 2016, the Company had UTBs of $8.3 million. Of this amount, $5.4 million would, if recognized, impact its effective tax rate, with the remaining amount being comprised of UTBs related to gross temporary differences or other indirect benefits. Pursuant to the Tax Sharing Agreement, Sears Holdings Corporation is generally responsible for all United States federal, state and local UTBs through the date of the Separation and, as such, an indemnification asset from Sears Holdings Corporation for the pre-Separation UTBs is recorded in Other assets in the Condensed Consolidated Balance Sheets. The indemnification asset was $14.4 million, $13.5 million and $13.7 million as of October 28, 2016, October 30, 2015, and January 29, 2016, respectively.

The Company classifies interest expense and penalties related to UTBs and interest income on tax overpayments as components of income tax expense. As of October 28, 2016, the total amount of interest expense and penalties recognized on our balance sheet was $6.4 million ($4.2 million net of federal benefit). The total amount of net interest expense recognized in the Condensed Consolidated Statements of Operations was insignificant for all periods presented. The Company files income tax returns in the United States and various foreign jurisdictions. The Company is under examination by various income tax jurisdictions for the years 2009 to 2015.

During the Third Quarter 2015, Sears Holdings settled tax audits in certain state tax jurisdictions related to pre-Separation periods. As a result, the Company re-evaluated the reserves for the pre-Separation period and recorded a

$1.2 million reduction in income tax expense, before consideration of federal income tax benefit. Under the Tax Sharing Agreement, Sears Holdings indemnifies the Company for such liabilities and, as a result, the Company reduced the indemnification receivable by $1.2 million; such reduction was reflected as a decrease in Other assets in the Condensed Consolidated Balance Sheets and as Other expense (income), net in the Condensed Consolidated and Combined Statements of Operations.

NOTE 9. COMMITMENTS AND CONTINGENCIES

Legal Proceedings

The Company is party to various claims, legal proceedings and investigations arising in the ordinary course of business. Some of these actions involve complex factual and legal issues and are subject to uncertainties. At this time, the Company is not able to either predict the outcome of these legal proceedings or reasonably estimate a potential range of loss with respect to the proceedings. While it is not feasible to predict the outcome of such pending claims, proceedings and investigations with certainty, management is of the opinion that their ultimate resolution should not have a material adverse effect on results of operations, cash flows or financial position taken as a whole.

Beginning in 2005, the Company initiated the first of several claims in Iowa County Circuit Court against the City of Dodgeville (the "City") to recover overpaid taxes resulting from the City’s excessive property tax assessment of the Company’s headquarters campus. In July 2016, the Company filed an amended and supplemental complaint to recover over paid property taxes for the 2016 tax year. As of November 30, 2016, the City has refunded, as the result of various court decisions, approximately $6.5 million in excessive taxes and interest to the Company in the following amounts: (1) approximately $1.6 million arising from the 2005 and 2006 tax years that was recognized in the fiscal year ended January 29, 2010; (2) approximately $1.6 million arising from the 2007, 2009 and 2010 tax years, recognized in the fiscal year ended January 31, 2014; (3) approximately $0.9 million arising from the 2008 tax year, recognized in the fiscal year ended January 30, 2015; (4) approximately $1.3 million arising from the 2011 and 2012 tax years, recognized in Second Quarter 2016; and (5) approximately $1.1 million arising from the 2007, 2009 and 2010 tax years, recognized in Third Quarter 2016; primarily within Selling and administrative costs in the Condensed Consolidated Statements of Operations.

The claims arising from the 2005 through 2010 and 2012 tax years are closed. The Company's claims arising from tax years 2011 and 2013 through 2016 remain unresolved and are still pending before the courts. The Company believes that the potential additional aggregate recovery from the City arising from the 2011 and 2013 through 2016 tax years will range from $0.7 million to $2.0 million, none of which has been recorded in the Condensed Consolidated Financial Statements.

NOTE 10. RELATED PARTY TRANSACTIONS

According to statements on form Schedule 13D filed with the SEC by ESL, ESL beneficially owned significant portions of both the Company's and Sears Holdings Corporation's outstanding shares of common stock. Therefore, Sears Holdings Corporation, the Company's former parent company, is considered a related party.

In connection with and subsequent to the Separation, the Company entered into various agreements with Sears Holdings which, among other things, (i) govern specified aspects of the Company's relationship following the Separation, especially with regards to the Lands’ End Shops at Sears, and (ii) establish terms pursuant to which subsidiaries of Sears Holdings Corporation are providing services to us.

See further descriptions of the transactions in the Company's 2015 Annual Report on Form 10-K and proxy statement filed with the SEC on April 1, 2016 . The components of the transactions between the Company and Sears Holdings, which exclude pass-through payments to third parties, are as follows:

Lands’ End Shops at Sears

Related party costs charged by Sears Holdings to the Company related to Lands’ End Shops at Sears are as follows:

(in thousands, except for number of stores)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Rent, CAM and occupancy costs	$6,165	$ 6,167	$18,707	$ 19,049
Retail services, store labor	6,004	6,774	18,034	20,051
Financial services and payment processing	573	627	1,963	1,876
Supply chain costs	183	219	735	768
Total expenses	$12,925	$ 13,787	$39,439	$ 41,744
Number of Lands’ End Shops at Sears at period end	219	227	219	227

General Corporate Services

Related party costs charged by Sears Holdings to the Company for general corporate services are as follows:

(in thousands)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Sourcing	$4,941	$ 3,632	$7,979	$ 7,670
Shop Your Way	596	751	1,670	2,007
Shared services	48	111	143	393
Total expenses	$5,585	$ 4,494	$9,792	$ 10,070

Sourcing

The Company contracts with a subsidiary of Sears Holdings to provide agreed upon buying agency services, on a non-exclusive basis, in foreign territories from where the Company purchases merchandise. These services, primarily based upon quantities purchased, include quality-control functions, regulatory compliance, product claims management and new vendor selection and setup assistance. During Second Quarter 2016 the Company entered into a new buying agency services agreement with a subsidiary of Sears Holding and terminated the agreement that was entered into at the time of the Separation. The new agreement provides for a higher commission rate and a higher annual commission minimum, as well as enhanced sourcing services, including for product development, costing analyses, vendor communications, vendor strategy and quality assurance. Certain of these amounts are capitalized into inventory and are expensed through cost of goods sold over the course of inventory turns and included in Cost of sales in the Condensed Consolidated Statements of Comprehensive Operations.

Use of Intellectual Property or Services

Related party revenue and costs charged by the Company to and from Sears Holdings for the use of intellectual property or services is as follows:

(in thousands)	13 Weeks Ended		39 Weeks Ended	
	October 28, 2016	October 30, 2015	October 28, 2016	October 30, 2015
Call center services	$492	$ 674	$1,459	$ 1,343
Lands' End business outfitters revenue	333	323	1,307	1,043
Credit card revenue	265	300	776	868
Royalty income	56	60	182	183
Gift card (expense)	(7)	(5)	(20)	(16)
Total income	$1,139	$ 1,352	$3,704	$ 3,421

Call Center Services

The Company has entered into a contract with Sears Holdings Management Corporation, a subsidiary of Sears Holdings Corporation, to provide call center services in support of Sears Holdings' SYW. This income is net of agreed upon costs directly attributable to the Company providing these services. The income is included in Net revenue and costs are included in Selling and administrative expenses in the Condensed Consolidated Statements of Operations. Total call center service income included in Net revenue was $2.0 million, $2.2 million, $5.8 million and $5.3 million for the Third Quarter 2016, Third Quarter 2015, Year to Date 2016 and Year to Date 2015, respectively.

Additional Balance Sheet Information

At October 28, 2016, October 30, 2015 and January 29, 2016 the Company included $4.6 million, $5.1 million and $3.9 million in Accounts receivable, net, respectively, and $3.8 million, $9.4 million and $2.7 million in Accounts payable, respectively, in the Condensed Consolidated Balance Sheets to reflect amounts due from and owed to Sears Holdings.

At October 28, 2016, October 30, 2015 and January 29, 2016 a $14.4 million, $13.5 million and $13.7 million receivable, respectively, was recorded by the Company in Other assets in the Condensed Consolidated Balance Sheets to reflect the indemnification by Sears Holdings Corporation of the pre-Separation UTBs (including penalties and interest) for which Sears Holdings Corporation is responsible under the Tax Sharing Agreement.

NOTE 11. SEGMENT REPORTING

The Company is a leading multi-channel retailer of clothing, accessories and footwear, as well as home products, and has two reportable segments: Direct and Retail. Both segments sell similar products and provide services. Product revenues are divided by product categories: Apparel and Non-apparel. The Non-apparel revenues include accessories, footwear, and home goods. Services and other revenue includes embroidery, monogramming, gift wrapping, shipping and other services. Net revenue is aggregated by product category in the following table:

(in thousands)	13 Weeks Ended		39 Weeks Ended	
	October 28, 2016	October 30, 2015	October 28, 2016	October 30, 2015
Net revenue:				
Apparel	$252,082	$272,228	$725,062	$783,841
Non-apparel	37,854	40,708	95,021	106,536
Service and other	21,540	21,498	56,836	55,858
Total net revenue	$311,476	$334,434	$876,919	$946,235

The Company identifies reportable segments according to how business activities are managed and evaluated. Each of the Company's operating segments are reportable segments and are strategic business units that offer similar products and services but are sold either directly from its warehouses (Direct) or through its retail stores (Retail).

Adjusted EBITDA is the primary measure used to make decisions on allocating resources and assessing performance of each operating segment. Adjusted EBITDA is computed as Income before taxes appearing on the Condensed Consolidated Statements of Operations net of interest expense, depreciation and amortization and other significant items that while periodically affecting the Company's results, may vary significantly from period to period and may have a disproportionate effect in a given period, which may affect comparability of results. Reportable segment assets are those directly used in or clearly allocable to an operating segment's operations. Depreciation, amortization, and property and equipment expenditures are recognized in each respective segment. There were no material transactions between reporting segments for any periods presented.

- The Direct segment sells products through the Company's e-commerce websites and direct mail catalogs. Operating costs consist primarily of direct marketing costs (catalog and e-commerce marketing costs); order processing and shipping costs; direct labor and benefits costs and facility costs. Assets primarily include goodwill and trade name intangible assets, inventory, accounts receivable, prepaid expenses (deferred catalog costs), technology infrastructure, and property and equipment.
- The Retail segment sells products and services through dedicated Lands' End Shops at Sears across the United States, the Company's stand-alone Lands' End Inlet stores and international shop-in-shops. Operating costs consist primarily of labor and benefits costs; rent, CAM and occupancy costs; distribution costs; and in-store marketing costs. Assets primarily include retail inventory, fixtures and leasehold improvements.
- Corporate overhead and other expenses include unallocated shared-service costs, which primarily consist of employee services and financial services, legal and corporate expenses. These expenses include labor and benefits costs, corporate headquarters occupancy costs and other administrative expenses. Assets include corporate headquarters and facilities, corporate cash and cash equivalents and deferred income taxes.

Financial information by segment is presented in the following tables.

SUMMARY OF SEGMENT DATA

	13 Weeks Ended		39 Weeks Ended	
(in thousands)	October 28, 2016	October 30, 2015	October 28, 2016	October 30, 2015
Net revenue:				
Direct	$272,080	$287,778	$750,660	805,886
Retail	39,340	46,597	126,077	140,166
Corporate / other	56	59	182	183
Total net revenue	$311,476	$334,434	$876,919	$946,235

	13 Weeks Ended		39 Weeks Ended	
(in thousands)	October 28, 2016	October 30, 2015	October 28, 2016	October 30, 2015
Adjusted EBITDA:				
Direct	$13,904	$36,951	$41,516	$85,316
Retail	(3,583)	(1,714)	(7,063)	(907)
Corporate / other	(9,035)	(8,689)	(25,271)	(25,191)
Total adjusted EBITDA	$1,286	$26,548	$9,182	$59,218

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(in thousands)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Depreciation and amortization:				
Direct	$4,027	$3,385	$11,097	$10,280
Retail	408	510	1,233	1,506
Corporate / other	360	365	1,089	1,088
Total depreciation and amortization	$4,795	$4,260	$13,419	$12,874

(in thousands)	October 28, 2016	October 30, 2015	January 29, 2016
Total Assets:			
Direct	$1,073,975	$1,166,991	$953,502
Retail	78,373	79,492	69,321
Corporate / other	160,830	135,536	258,703
Total assets	$1,313,178	$1,382,019	$1,281,526

(in thousands)	13 Weeks Ended October 28, 2016	13 Weeks Ended October 30, 2015	39 Weeks Ended October 28, 2016	39 Weeks Ended October 30, 2015
Capital expenditures:				
Direct	$8,041	$4,415	$25,804	$17,717
Retail	25	95	279	148
Corporate / other	—	87	—	252
Total capital expenditures	$8,066	$4,597	$26,083	$18,117

NOTE 12. RECENT ACCOUNTING PRONOUNCEMENTS

Simplifying the Measurement of Inventory

In July 2015, the FASB issued ASU 2015-11, Simplifying the Measurement of Inventory. Under this ASU, non-LIFO inventory will be measured at the lower of cost and net realizable value, eliminating the options that currently exist for market valuation. The ASU defines net realizable value as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. No other changes were made to the current guidance on inventory measurement. This guidance was effective for Lands' End in the First Quarter 2016 and only applies to our international inventory as United States inventory is valued using LIFO. The adoption of this guidance did not have a material impact on the Company's Condensed Consolidated Financial Statements.

Customer's Accounting for Fees Paid in a Cloud Computing Arrangement

In April 2015, the FASB issued ASU 2015-05, Customers' Accounting for Fees Paid in a Cloud Computing Arrangement, which clarifies the circumstances under which a cloud computing customer would account for the arrangement as a license of internal-use software under ASC 350-40. This guidance was effective for Lands' End in the First Quarter 2016. The adoption of this guidance did not have a material impact on the Company's Condensed Consolidated Financial Statements.

Simplifying the Presentation of Debt Issuance Costs

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which changed the required presentation of debt issuance costs from an asset on the balance sheet to a deduction from the related debt liability. This guidance was adopted by the Company during First Quarter 2016. See Note 4, Debt, for further discussion.

Revenue from Contracts with Customers
In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which provides guidance for revenue recognition. The standard’s core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under today’s guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. This guidance was deferred by ASU 2015-14, Revenue from Contracts with Customers, issued by the FASB in August 2015, and will be effective for Lands' End in the first quarter of its fiscal year ending February 1, 2019. Subsequently, the FASB has also issued accounting standards updates which clarify the guidance. The Company is currently in the process of evaluating the impact of adoption of this ASU and related clarifications on the Company's Condensed Consolidated Financial Statements.
Compensation - Stock Compensation
In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation, which simplifies the accounting for the taxes related to stock based compensation, including adjustments to how excess tax benefits and a company's payments for tax withholdings should be classified. This guidance will be effective for Lands' End in the first quarter of its fiscal year ending February 2, 2018. The adoption of this guidance is not expected to have a material impact on the Company's Condensed Consolidated Financial Statements.
Recognition of Breakage for Certain Prepaid Stored-Value Products
In March 2016, the FASB issued ASU 2016-04, Recognition of Breakage for Certain Prepaid Stored-Value Products. This update clarifies when it is acceptable to recognize the unredeemed portion of prepaid gift cards into income. This guidance will be effective for Lands' End in the first quarter of its fiscal year ending February 1, 2019. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's Condensed Consolidated Financial Statements.
Classification of Certain Cash Receipts and Cash Payments
In August 2016, the FASB issued ASU 2016-15, Classification of Certain Cash Receipts and Cash Payments. This update clarifies issues to reduce the current and potential future diversity in practice of the classification of certain cash receipts and cash payments within the statement of cash flows. This guidance will be effective for Lands' End in the first quarter of its fiscal year ending February 1, 2019. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's Condensed Consolidated Financial Statements.
Leases
In February 2016, the FASB issued ASU 2016-02, Leases, which will replace the existing guidance in ASC 840, Leases. This ASU requires a dual approach for lessee accounting under which a lessee would account for leases as finance leases or operating leases. Both finance leases and operating leases will result in the lessee recognizing a right-of-use asset and a corresponding lease liability. For finance leases, the lessee would recognize interest expense and amortization of the right-of-use asset, and for operating leases, the lessee would recognize a straight-line total lease expense. This guidance will be effective for Lands' End in the first quarter of its fiscal year ending January 31, 2020. The Company is currently in the process of evaluating the impact of adoption of this ASU on the Company's Condensed Consolidated Financial Statements.

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

You should read the following discussion in conjunction with the Condensed Consolidated Financial Statements and accompanying notes included elsewhere in this Quarterly Report on Form 10-Q. This Management’s Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements. The matters discussed in these forward-looking statements are subject to risk, uncertainties, and other factors that could cause actual results to differ materially from those made, projected or implied in the forward-looking statements. See “Cautionary Statements Concerning Forward-Looking Statements” below and "Item 1A. Risk Factors" in our Annual Report filed on Form 10-K for the year ended January 29, 2016, for a discussion of the uncertainties, risks and assumptions associated with these statements.

As used in this Quarterly Report on Form 10-Q, references to the “Company”, “Lands' End”, “we”, “us”, “our” and similar terr refer to Lands' End, Inc. and its subsidiaries. Our fiscal year ends on the Friday preceding the Saturday closest to January 31. Other terms that are commonly used in this Quarterly Report on Form 10-Q are defined as follows:

- ABL Facility - Asset-based senior secured credit agreements, dated as of April 4, 2014, with Bank of America, N.A and certain other lenders
- Debt Facilities - Collectively, the ABL Facility and the Term Loan Facility
- ERP - Enterprise resource planning software solutions
- ESL - ESL Investments, Inc. and its investment affiliates, including Edward S. Lampert
- Fiscal 2016 - the fifty-two weeks ending January 27, 2017
- Fiscal 2015 - the fifty-two weeks ended January 29, 2016
- Fiscal November 2016 - the four week fiscal month ending November 25, 2016
- Fourth Quarter 2015 - The thirteen weeks ended January 29, 2016
- GAAP - Accounting principles generally accepted in the United States
- Same Store Sales - Net sales, from stores that have been open for at least 12 full months where selling square footage has not changed by 15% or more within the past fiscal year
- Sears Holdings or Sears Holdings Corporation - Sears Holdings Corporation, a Delaware Corporation, and its consolidated subsidiaries (other than, for all periods following the Separation, Lands' End)
- Sears Roebuck - Sears, Roebuck and Co., a subsidiary of Sears Holdings Corporation
- SEC - United States Securities and Exchange Commission
- Second Quarter 2016 - The thirteen weeks ended July 29, 2016
- Separation - On April 4, 2014 Sears Holdings distributed 100% of the outstanding common stock of Lands' End to its shareholders
- Term Loan Facility - Term loan credit agreements, dated as of April 4, 2014, with Bank of America, N.A. and certain other lenders
- Third Quarter 2016 - the thirteen weeks ended October 28, 2016
- Third Quarter 2015 - the thirteen weeks ended October 30, 2015
- UK Borrower - A United Kingdom subsidiary borrower of Lands’ End under the ABL Facility
- Year to Date 2016 - the thirty-nine weeks ended October 28, 2016
- Year to Date 2015 - the thirty-nine weeks ended October 30, 2015

Introduction

Management's discussion and analysis of financial condition and results of operations accompanies our Condensed Consolidated Financial Statements and provides additional information about our business, financial condition, liquidity and capital resources, cash flows and results of operations. We have organized the information as follows:

- Executive overview. This section provides a brief description of our business, accounting basis of presentation and a brief summary of our results of operations.
- Discussion and analysis. This section highlights items affecting the comparability of our financial results and provides an analysis of our segment results of operations for the 2016 and 2015 third fiscal quarter and fiscal year to date periods.
- Liquidity and capital resources. This section provides an overview of our historical and anticipated cash and financing activities. We also review our historical sources and uses of cash in our operating, investing and financing activities.
- Contractual Obligations and Off-Balance-Sheet Arrangements. This section provides details of the Company's off-balance-sheet arrangements and contractual obligations for the next five years and thereafter.
- Financial Instruments with Off-Balance-Sheet Risk. This section discusses financial instruments of the Company that could have off-balance-sheet risk.
- Application of critical accounting policies and estimates. This section summarizes the accounting policies that we consider important to our financial condition and results of operations and which require significant judgment or estimates to be made in their application.
- Recent accounting pronouncements. This section summarizes recently issued accounting pronouncements and the impact or expected impact on the Company's financial statements.

Executive Overview

Description of the Company

Lands’ End, Inc. is a leading multi-channel retailer of clothing, accessories and footwear, as well as home products. We offer products through catalogs, online at www.landsend.com, www.canvasbylandsend.com and affiliated specialty and international websites, and through retail locations, primarily at Lands’ End Shops at Sears, stand-alone Lands’ End Inlet stores and international shop-in-shops that sell merchandise in various retail department stores. We are a classic American lifestyle brand with a passion for quality, legendary service and real value, and we seek to deliver timeless style for men, women, kids and the home. Lands’ End was founded in 1963 in Chicago by Gary Comer and his partners to sell sailboat hardware and equipment by catalog. While our product focus has shifted significantly over the years, we have continued to adhere to our founder’s motto as one of our guiding principles: “Take care of the customer, take care of the employee and the rest will take care of itself.”

The Company identifies reportable segments according to how business activities are managed and evaluated. Each of the Company’s operating segments are reportable segments and are strategic business units that offer similar products and services but are sold either directly from our warehouses (Direct) or through our retail stores (Retail).

Basis of Presentation

The Condensed Consolidated Financial Statements include the accounts of Lands' End, Inc. and its subsidiaries. All intercompany transactions and balances have been eliminated.

Following the Separation, we began operating as a separate, publicly traded company, independent from Sears Holdings. According to statements on form Schedule 13D filed with the SEC by ESL, ESL beneficially owned significant portions of both the Company's and Sears Holdings Corporation's outstanding shares of common stock. Therefore Sears Holdings Corporation, the Company's former parent company, is considered a related party both prior to and subsequent to the Separation.

The success of our Retail segment depends on the performance of the Lands’ End Shops at Sears. Under the terms of the master lease agreement and master sublease agreement pursuant to which Sears Roebuck leases or subleases to us the premises for the Lands’ End Shops at Sears, Sears Roebuck has certain rights to (1) relocate our leased premises within the building in which such premises are located, subject to certain limitations, including our right to terminate the applicable lease if we are not satisfied with the new premises, and (2) terminate without liability the lease with respect to a particular

Lands' End Shop if the overall Sears store in which such Lands' End Shop is located is closed or sold. Sears Holdings announced that it intends to continue to right-size, redeploy and highlight the value of its assets, including its real estate portfolio, in its transition from an asset-intensive, store-focused retailer and that it has entered into lease agreements with third party retailers for stand-alone stores. On July 7, 2015, Sears Holdings completed a rights offering and sale-leaseback transaction (the "Seritage transaction") with Seritage Growth Properties ("Seritage"), an independent publicly traded real estate investment trust. Sears Holdings disclosed that as part of the Seritage transaction, it sold 235 properties to Seritage (the "REIT properties") along with Sears Holdings' 50% interest in each of three real estate joint ventures (collectively, the "JVs"). Sears Holdings also disclosed that it contributed 31 properties to the JVs (the "JV properties"). As of October 28, 2016, 55 of the REIT properties contained a Lands' End Shop and 15 of the JV properties contained a Lands' End Shop, the leases with respect to which Sears Roebuck retained for its own account. Sears Holdings disclosed that Seritage and the JVs have a recapture right with respect to approximately 50% of the space within the stores at the REIT properties and JV properties (subject to certain exceptions), and with respect to eight of the stores that contain a Lands' End Shop, Seritage has the additional right to recapture 100% of the space within the Sears Roebuck store. If Sears Roebuck continues to dispose of retail stores that contain Lands' End Shops, and/or offer us relocation alternatives for Lands' End Shops that are less attractive than the current premises, our business and results of operations could be adversely affected. On October 28, 2016 the Company operated 219 Lands' End Shops at Sears, compared with 227 Lands' End Shops at Sears on October 30, 2015.

Seasonality

We experience seasonal fluctuations in our Net revenue and operating results and historically have realized a significant portion of our net sales and earnings for the year during our fourth fiscal quarter. We generated approximately 34% of our Net revenue in the fourth fiscal quarter of the past three years. Thus, lower than expected fourth quarter net revenue could have an adverse impact on our annual operating results.

Working capital requirements typically increase during the third quarter of the fiscal year as inventory builds to support peak shipping/selling period and, accordingly, typically decrease during the fourth quarter of the fiscal year as inventory is shipped/sold. Cash provided by operating activities is typically higher in the fourth quarter of the fiscal year due to reduced working capital requirements during that period.

Results of Operations

The following table sets forth, for the periods indicated, selected income statement data:

	13 Weeks Ended			
	October 28, 2016		October 30, 2015	
(in thousands)	$'s	% of Net revenue	$'s	% of Net revenue
Net revenue	$311,476	100.0 %	$334,434	100.0 %
Cost of sales (excluding depreciation and amortization)	177,825	57.1 %	172,019	51.4 %
Gross profit	133,651	42.9 %	162,415	48.6 %
Selling and administrative	132,365	42.5 %	135,867	40.6 %
Depreciation and amortization	4,795	1.5 %	4,260	1.3 %
Other operating (income), net	(86)	— %	(1,009)	(0.3)%
Operating (loss) income	(3,423)	(1.1)%	23,297	7.0 %
Interest expense	6,149	2.0 %	6,204	1.9 %
Other (income) expense, net	(432)	(0.1)%	796	0.2 %
(Loss) income before income taxes	(9,140)	(2.9)%	16,297	4.9 %
Income tax (benefit) expense	(1,918)	(0.6)%	5,572	1.7 %
NET (LOSS) INCOME	$(7,222)	(2.3)%	$10,725	3.2 %

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	39 Weeks Ended			
	October 28, 2016		October 30, 2015	
(in thousands)	$'s	% of Net revenue	$'s	% of Net revenue
Net revenue	$876,919	100.0 %	$946,235	100.0 %
Cost of sales (excluding depreciation and amortization)	477,446	54.4 %	492,756	52.1 %
Gross profit	399,473	45.6 %	453,479	47.9 %
Selling and administrative	390,291	44.5 %	394,261	41.7 %
Depreciation and amortization	13,419	1.5 %	12,874	1.4 %
Other operating (income), net	(40)	— %	(3,366)	(0.4)%
Operating (loss) income	(4,197)	(0.5)%	49,710	5.3 %
Interest expense	18,493	2.1 %	18,615	2.0 %
Other (income) expense, net	(1,413)	(0.2)%	(210)	— %
(Loss) income before income taxes	(21,277)	(2.4)%	31,305	3.3 %
Income tax (benefit) expense	(6,316)	(0.7)%	11,395	1.2 %
NET (LOSS) INCOME	$(14,961)	(1.7)%	$19,910	2.1 %

Depreciation and amortization is not included in our cost of sales because we are a reseller of inventory and do not believe that including depreciation and amortization is meaningful. As a result, our gross margins may not be comparable to other entities that include depreciation and amortization related to the sale of their product in their gross margin measure.

Net (Loss) Income and Adjusted EBITDA

We recorded a Net loss of $7.2 million in the Third Quarter 2016 compared to a Net income of $10.7 million in the Third Quarter 2015. In addition to our Net (loss) income determined in accordance with GAAP, for purposes of evaluating operating performance, we use an Adjusted EBITDA measurement. Adjusted EBITDA is computed as Net (loss) income appearing on the Condensed Consolidated Statements of Operations net of Income tax (benefit) expense, Other income, net, Interest expense, Depreciation and amortization, and certain significant items set forth below. Our management uses Adjusted EBITDA to evaluate the operating performance of our businesses, as well as executive compensation metrics, for comparable periods. Adjusted EBITDA should not be used by investors or other third parties as the sole basis for formulating investment decisions as it excludes a number of important cash and non-cash recurring items.

While Adjusted EBITDA is a non-GAAP measurement, management believes that it is an important indicator of operating performance, and useful to investors, because:

- EBITDA excludes the effects of financings, investing activities and tax structure by eliminating the effects of interest, depreciation and income tax costs or benefits.
- Other significant items, while periodically affecting our results, may vary significantly from period to period and have a disproportionate effect in a given period, which affects comparability of results. We have adjusted our results for these items to make our statements more comparable and therefore more useful to investors as the items are not representative of our ongoing operations.

We excluded a benefit related to the reversal of a portion of the product recall accrual recognized in Fiscal 2014 as this was an unusual event that affects the comparability of our financial results.

We excluded the gain or loss on disposal of property and equipment as management considers the gains or losses on disposal of assets to result from investing decisions rather than ongoing operations.

	13 Weeks Ended			
	October 28, 2016		October 30, 2015	
(in thousands)	$'s	% of Net revenue	$'s	% of Net revenue
Net (loss) income	$(7,222)	(2.3)%	$10,725	3.2%
Income tax (benefit) expense	(1,918)	(0.6)%	5,572	1.7%
Other (income) expense, net	(432)	(0.1)%	796	0.2%
Interest expense	6,149	2.0%	6,204	1.9%
Operating (loss) income	(3,423)	(1.1)%	23,297	7.0%
Depreciation and amortization	4,795	1.5%	4,260	1.3%
Product recall	(212)	(0.1)%	(1,007)	(0.3)%
Loss (gain) on disposal of property and equipment	126	—%	(2)	—%
Adjusted EBITDA	$1,286	0.4%	$26,548	7.9%

	39 Weeks Ended			
	October 28, 2016		October 30, 2015	
(in thousands)	$'s	% of Net revenue	$'s	% of Net revenue
Net (loss) income	$(14,961)	(1.7)%	$19,910	2.1%
Income tax (benefit) expense	(6,316)	(0.7)%	11,395	1.2%
Other (income) expense, net	(1,413)	(0.2)%	(210)	—%
Interest expense	18,493	2.1%	18,615	2.0%
Operating (loss) income	(4,197)	(0.5)%	49,710	5.3%
Depreciation and amortization	13,419	1.5%	12,874	1.4%
Product recall	(212)	—%	(3,371)	(0.4)%
Loss on disposal of property and equipment	172	—%	5	—%
Adjusted EBITDA	$9,182	1.0%	$59,218	6.3%

In assessing the operational performance of our business, we consider a variety of financial measures. We operate in two reportable segments, Direct (sold through e-commerce websites and direct mail catalogs) and Retail (sold through stores). A key measure in the evaluation of our business is revenue performance by segment. We also consider gross margin and Selling and administrative expenses in evaluating the performance of our business.

To evaluate revenue performance for the Direct segment we use Net revenue. For our Retail segment, we use Same Store Sales as a key measure in evaluating performance. A store is included in Same Store Sales calculations on the first day it has comparable prior year sales. Stores in which the selling square footage has changed by 15% or more as a result of a remodel, expansion, reduction or relocation are excluded from Same Store Sales calculations until the first day they have comparable prior year sales. Online sales and sales generated through our in-store computer kiosks are considered revenue in our Direct segment and are excluded from Same Store Sales.

Discussion and Analysis

Third Quarter 2016 compared with the Third Quarter 2015

Net Revenue

Net revenue for the Third Quarter 2016 was $311.5 million, compared with $334.4 million in the comparable period of the prior year, a decrease of $23.0 million or 6.9%. The decrease was comprised of a decrease in our Direct segment of $15.7 million and a decrease in our Retail segment of $7.3 million.

Net revenue in our Direct segment was $272.1 million for the Third Quarter 2016, a decrease of $15.7 million, or 5.5% from the comparable period of the prior year. The decrease in the Direct segment was a continuation of the difficult retail environment which led us to broaden our promotional activity with deeper discounting. The Direct segment did, however,

experience an incremental improvement from Second Quarter 2016 as the Company increased catalog circulation and improved catalog presentation. During the quarter our uniform business out performed the rest of the Direct segment.

Net revenue in our Retail segment was $39.3 million for the Third Quarter 2016, a decrease of $7.3 million, or 15.6% from the comparable period of the prior year. The decrease was driven by a 14.3% decrease in Same Store Sales, and a decrease in the number of Lands' End Shops at Sears. The Same Store Sales decrease was attributable to the same competitive marketplace as in our Direct segment as well as declining traffic at our Lands' End Shops at Sears. On October 28, 2016, the Company operated 219 Lands' End Shops at Sears, 14 global Lands' End Inlet stores and no international shop-in-shops compared with 227 Lands' End Shops at Sears, 14 global Lands' End Inlet stores and five international shop-in-shops on October 30, 2015.

Gross Profit

Total gross profit decreased $28.8 million to $133.7 million and gross margin decreased approximately 570 basis points to 42.9% of total Net revenue in the Third Quarter 2016, compared with $162.4 million, or 48.6% of total Net revenue, in the Third Quarter 2015. The gross profit decrease was comprised of a decrease in our Direct segment of $25.2 million and a decrease in our Retail segment of $3.6 million.

Gross profit in the Direct segment was $116.7 million compared with $141.9 million for the Third Quarter 2016 and Third Quarter 2015, respectively. Gross margin in the Direct segment decreased approximately 640 basis points to 42.9% in the Third Quarter 2016 versus 49.3% in the comparable prior year period. The decrease in Gross margin during the third quarter was primarily attributable to increased promotional activity in the highly competitive retail environment. Additionally, approximately 160 basis points of the decrease resulted from a $4.4 million write down of under performing Canvas by Lands' End inventory.

Retail segment gross profit decreased $3.6 million to $16.9 million in the Third Quarter 2016 from $20.5 million in the Third Quarter 2015. Retail segment gross margin decreased to 42.9% for the Third Quarter 2016 compared to 44.0% for the Third Quarter 2015 driven by increased promotional activity to remain competitive in current retail environment.

Selling and Administrative Expenses

Selling and administrative expenses were $132.4 million, or 42.5% of total Net revenue compared with $135.9 million or 40.6% of total Net revenue in the Third Quarter 2016 and Third Quarter 2015, respectively. During the quarter we incurred $1.2 million of expenses associated with the departure of the Company's former Chief Executive Officer. The decrease in Selling and administrative expenses was primarily due to a decrease of $2.1 million in the Direct segment, a decrease of $1.7 million in the Retail segment and an increase of $0.3 million in the Corporate segment.

The Direct segment Selling and administrative expenses were $102.8 million compared with $104.9 million for the Third Quarter 2016 and Third Quarter 2015, respectively. The $2.1 million or 2.0% decrease, was primarily attributable to a property tax recovery related to our claims and ongoing litigation against the City of Dodgeville and lower variable costs resulting from lower revenue.

The Retail segment Selling and administrative expenses were $20.5 million compared with $22.2 million for the Third Quarter 2016 and Third Quarter 2015, respectively. The $1.7 million or 8.0% decrease was primarily attributable to a decrease in marketing investments and personnel costs.

Corporate / other Selling and administrative expenses increased to $9.1 million in the Third Quarter 2016 compared to $8.8 million in the Third Quarter 2015 due to increased severance expenses resulting from the CEO transition, partially offset by a decrease in other personnel costs.

Depreciation and Amortization

Depreciation and amortization expense was $4.8 million in the Third Quarter 2016, an increase of $0.5 million or 12.6%, compared with $4.3 million in Third Quarter 2015, primarily attributable to an increase in depreciation associated with acquired information technology assets.

Other Operating (Income), Net

The decrease in Other operating income, net was attributable to the Third Quarter 2015 reversal of approximately $1.0 million of the product recall accrual that was recorded in Fourth Quarter 2014.

Operating (Loss) Income

Operating (loss) income decreased to a $3.4 million loss in the Third Quarter 2016 from $23.3 million of income in Third Quarter 2015 primarily due to lower revenues and lower gross margin discussed above.

Interest Expense

Interest expense was essentially unchanged at $6.1 million in the Third Quarter 2016 compared to $6.2 million in the Third Quarter 2015.

Other (Income) / Expense, Net

Other (Income) / Expense, Net in the Third Quarter 2015 includes a charge of $1.2 million from the reduction to a tax receivable from our former parent as a result of favorable tax settlements in certain tax jurisdictions.

Income Tax (Benefit) Expense

Income tax benefit was $1.9 million for the Third Quarter 2016 compared with income tax expense of $5.6 million in the Third Quarter 2015. The decrease was primarily attributable to a Net loss in comparison to Net income in the prior year. The effective tax rate was 21.0% in the Third Quarter 2016 compared with 34.2% in the Third Quarter 2015. The change is primarily attributable to the effects of credits and other permanent differences for the Company.

Net (Loss) Income

As a result of the above factors, Net loss was $7.2 million and diluted loss per share was $0.23 in the Third Quarter 2016 compared with Net income of $10.7 million and diluted earnings per share of $0.33 in the Third Quarter 2015. Net loss for the Third Quarter 2016 includes the aforementioned $4.4 million inventory write-down ($3.0 million net of tax), as well as $1.2 million in one-time personnel costs net of reversals ($0.8 million net of tax), primarily related to the departure of the Company's former Chief Executive Officer.

Adjusted EBITDA

As a result of the above factors, Adjusted EBITDA decreased to $1.3 million in the Third Quarter 2016 from $26.5 million in the Third Quarter 2015.

Year to Date 2016 compared with the Year to Date 2015

Net Revenue

Net revenue for the Year to Date 2016 was $876.9 million, compared with $946.2 million in the comparable period of the prior year, a decrease of $69.3 million or 7.3%. The decrease was comprised of a decrease in our Direct segment of $55.2 million and a decrease in our Retail segment of $14.1 million.

Net revenue in our Direct segment was $750.7 million for the Year to Date 2016, a decrease of $55.2 million, or 6.9% from the comparable period of the prior year. The decrease was attributable to declines in all of our markets, though primarily concentrated in our U.S. consumer business. We realized declining performance in most of our major product categories, as the highly competitive and promotional retail environment negatively impacted our ability to generate traffic to our U.S. consumer websites.

Net revenue in our Retail segment was $126.1 million for the Year to Date 2016, a decrease of $14.1 million, or 10.1% from the comparable period of the prior year. The decrease was driven by a 7.9% decrease in Same Store Sales, and a decrease in the number of Lands’ End Shops at Sears. The Same Store Sales decrease was attributable to the same competitive marketplace as in our Direct segment as well as declining traffic at our Lands' End Shops at Sears. On October 28, 2016, the

Company operated 219 Lands' End Shops at Sears, 14 global Lands' End Inlet stores and no international shop-in-shops compared with 227 Lands' End Shops at Sears, 14 global Lands' End Inlet stores and five international shop-in-shops on October 30, 2015.

Gross Profit

Total gross profit decreased $54.0 million to $399.5 million and gross margin decreased approximately 230 basis points to 45.6% of total Net revenue, compared with $453.5 million, or 47.9% of total Net revenue, for the Year to Date 2016 and Year to Date 2015, respectively.

Gross profit in the Direct segment was $346.0 million compared with $390.5 million for the Year to Date 2016 and Year to Date 2015, respectively. The decrease in Gross profit is largely attributable to lower revenue. Gross margin in the Direct segment decreased approximately 240 basis points to 46.1% in the Year to Date 2016 versus 48.5% in the comparable prior year period, primarily attributable to a highly competitive retail environment resulting in increased promotional activity and deeper product discounts. Additionally, approximately 60 basis points of the decrease resulted from a $4.4 million write down of under performing Canvas by Lands' End inventory.

Retail segment gross profit decreased $9.5 million to $53.3 million in the Year to Date 2016 from $62.8 million in the Year to Date 2015. Retail segment gross margin decreased approximately 260 basis points to 42.2% compared with 44.8% for the Year to Date 2016 and Year to Date 2015, respectively, driven by the same factors which impacted our Direct segment.

Selling and Administrative Expenses

Selling and administrative expenses were $390.3 million, or 44.5% of total Net revenue compared with $394.3 million or 41.7% of total Net revenue in the Year to Date 2016 and Year to Date 2015, respectively. The $4.0 million decrease was attributable to a $0.7 million decrease in the Direct segment, a $3.4 million decrease in the Retail segment, and the Corporate segment was essentially flat.

The Direct segment Selling and administrative expenses were $304.5 million compared with $305.2 million for the Year to Date 2016 and Year to Date 2015, respectively. The $0.7 million or 0.2% decrease was primarily attributable to property tax recoveries related to our claims and ongoing litigation against the City of Dodgeville, partially offset by increased marketing investments.

The Retail segment Selling and administrative expenses were $60.3 million compared with $63.7 million for the Year to Date 2016 and Year to Date 2015, respectively. The $3.4 million or 5.3% decrease was primarily attributable to a decrease in personnel expenses, and expenses related to closed stores.

Corporate / other Selling and administrative expenses were $25.5 million compared with $25.4 million for the Year to Date 2016 and Year to Date 2015, respectively.

Depreciation and Amortization

Depreciation and amortization expense increased to $13.4 million in the Year to Date 2016 compared to $12.9 million in the Year to Date 2015, primarily attributable to an increase in depreciation associated with acquired information technology assets.

Other Operating (Income), Net

The decrease in Other Operating (Income), Net was attributable to the Third Quarter 2015 reversal of approximately $3.4 million of the product recall accrual that was recorded in Fourth Quarter 2014.

Operating (Loss) Income

Operating (loss) income decreased to a $4.2 million Operating loss in Year to Date 2016 from Operating income of $49.7 million in Year to Date 2015 primarily due to lower revenues and lower gross margin discussed above.

Interest Expense

Interest expense is essentially unchanged at $18.5 million in the Year to Date 2016 compared with $18.6 million in the Year to Date 2015.

Other (Income) / Expense, Net

Other (Income) / Expense, Net in the Year to Date 2015 includes a charge of $1.2 million from the reduction to a tax receivable from our former parent as a result of favorable tax settlements in certain tax jurisdictions.

Income Tax (Benefit) Expense