

Vera Bradley, Inc.  
Form 10-Q  
September 09, 2015  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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

For the Quarterly Period Ended August 1, 2015  
OR

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

For the Transition Period From \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number: 001-34918

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VERA BRADLEY, INC.  
(Exact name of registrant as specified in its charter)

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Indiana 27-2935063  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

12420 Stonebridge Road, 46783  
Roanoke, Indiana  
(Address of principal executive offices) (Zip Code)

(877) 708-8372  
(Registrant's telephone number, including area code)

None  
(Former name, former address and former fiscal year, if changed since last report)

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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.

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Large accelerated filer      ☐      Accelerated filer      ☒

Non-accelerated filer      ☐ (Do not check if a smaller reporting company)      Smaller reporting company      ☐

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

The registrant had 37,972,235 shares of its common stock outstanding as of September 9, 2015.

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**FORWARD-LOOKING STATEMENTS**

This report contains forward-looking statements that are subject to risks and uncertainties. All statements other than statements of historical or current fact included in this report are forward-looking statements. Forward-looking statements refer to our current expectations and projections relating to our financial condition, results of operations, plans, objectives, strategies, future performance, and business. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as “anticipate,” “estimate,” “expect,” “project,” “plan,” “intend,” “believe,” “may,” “might,” “will,” “should,” “can have,” and “li” words and terms of similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. For example, all statements we make relating to our estimated and projected earnings, revenues, costs, expenditures, cash flows, growth rates, and financial results, our plans and objectives for future operations, growth, initiatives, or strategies, or the expected outcome or impact of pending or threatened litigation are forward-looking statements. All forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those that we expected, including:

- possible inability to successfully implement our long-term strategic plan;
- possible failure of our multi-channel distribution model;
- possible adverse changes in general economic conditions and their impact on consumer confidence and consumer spending;
- possible inability to predict and respond in a timely manner to changes in consumer demand;
- possible inability to successfully open new stores and/or operate current stores as planned;
- possible inability to maintain and enhance our brand;
- possible loss of key management or design associates or inability to attract and retain the talent required for our business;
- possible data security or privacy breaches or disruptions in our computer systems or website; and
- possible continued declines in our comparable sales.

We derive many of our forward-looking statements from our operating plans and forecasts, which are based upon detailed assumptions. While we believe that our assumptions are reasonable, we caution that it is difficult to predict the impact of known factors, and it is impossible for us to anticipate all factors that could affect our actual results. For a discussion of these risks and other risks and uncertainties that could cause actual results to differ materially from those contained in our forward-looking statements, please refer to “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2015.

We caution you that the risks and uncertainties identified by us may not be all of the factors that are important to you. Furthermore, the forward-looking statements included in this report are made only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events, or otherwise, except as required by law.

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Vera Bradley, Inc.  
Consolidated Balance Sheets  
(in thousands)  
(unaudited)

	August 1, 2015	January 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$76,042	\$112,292
Accounts receivable, net	33,863	31,374
Inventories	103,921	98,403
Income taxes receivable	3,199	3,208
Prepaid expenses and other current assets	10,620	9,100
Deferred income taxes	13,473	13,320
Total current assets	241,118	267,697
Property, plant, and equipment, net	115,013	109,003
Other assets	1,046	584
Total assets	\$357,177	\$377,284
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	\$28,734	\$32,906
Accrued employment costs	10,264	14,595
Other accrued liabilities	15,107	15,548
Income taxes payable	286	—
Total current liabilities	54,391	63,049
Deferred income taxes	6,163	5,297
Other long-term liabilities	29,057	24,467
Total liabilities	89,611	92,813
Commitments and contingencies		
Shareholders' equity:		
Preferred stock; 5,000 shares authorized, no shares issued or outstanding	—	—
Common stock, without par value; 200,000 shares authorized, 40,790 and 40,695 shares issued and 38,595 and 40,074 outstanding, respectively	—	—
Additional paid-in-capital	83,023	80,992
Retained earnings	218,030	216,451
Accumulated other comprehensive loss	(14	) (15
Treasury stock	(33,473	) (12,957
Total shareholders' equity	267,566	284,471
Total liabilities and shareholders' equity	\$357,177	\$377,284
The accompanying notes are an integral part of these financial statements.		

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Vera Bradley, Inc.  
Consolidated Statements of Income  
(in thousands, except per share data)  
(unaudited)

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Net revenues	\$120,724	\$118,960	\$221,828	\$231,157
Cost of sales	54,170	55,516	103,580	107,958
Gross profit	66,554	63,444	118,248	123,199
Selling, general, and administrative expenses	57,351	50,663	114,963	100,708
Other income	283	465	1,230	2,042
Operating income	9,486	13,246	4,515	24,533
Interest expense, net	72	24	149	104
Income from continuing operations before income taxes	9,414	13,222	4,366	24,429
Income tax expense	3,699	5,328	2,787	9,658
Income from continuing operations	5,715	7,894	1,579	14,771
Loss from discontinued operations, net of taxes	—	(296	) —	(606
Net income	\$5,715	\$7,598	\$1,579	\$14,165
Basic weighted-average shares outstanding	39,315	40,686	39,600	40,663
Diluted weighted-average shares outstanding	39,328	40,719	39,606	40,722
Net income per share - basic				
Continuing operations	\$0.15	\$0.19	\$0.04	\$0.36
Discontinued operations	—	(0.01	) —	(0.01
Net income	\$0.15	\$0.19	\$0.04	\$0.35
Net income per share - diluted				
Continuing operations	\$0.15	\$0.19	\$0.04	\$0.36
Discontinued operations	—	(0.01	) —	(0.01
Net income	\$0.15	\$0.19	\$0.04	\$0.35

The accompanying notes are an integral part of these financial statements.

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Vera Bradley, Inc.  
 Consolidated Statements of Comprehensive Income  
 (in thousands)  
 (unaudited)

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Net income	\$5,715	\$7,598	\$1,579	\$14,165
Cumulative translation adjustment	(9	) (20	) 1	(10
Comprehensive income	\$5,706	\$7,578	\$1,580	\$14,155

The accompanying notes are an integral part of these financial statements.

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Vera Bradley, Inc.  
Consolidated Statements of Cash Flows  
(in thousands)  
(unaudited)

	Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014
Cash flows from operating activities		
Net income	\$1,579	\$14,165
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation of property, plant, and equipment	9,904	7,150
Provision for doubtful accounts	436	(63)
Loss on disposal of property, plant, and equipment	52	—
Stock-based compensation	2,515	1,962
Deferred income taxes	713	(2,007)
Changes in assets and liabilities:		
Accounts receivable	(2,925)	(895)
Inventories	(5,518)	24,897
Prepaid expenses and other assets	(1,982)	704
Accounts payable	(5,931)	(11,271)
Income taxes	295	(5,477)
Accrued and other liabilities	(136)	3,591
Net cash (used in) provided by operating activities	(998)	32,756
Cash flows from investing activities		
Purchases of property, plant, and equipment	(15,359)	(12,231)
Net cash used in investing activities	(15,359)	(12,231)
Cash flows from financing activities		
Tax withholdings for equity compensation	(484)	(595)
Repurchase of common stock	(19,364)	—
Other financing activities, net	(46)	(47)
Net cash used in financing activities	(19,894)	(642)
Effect of exchange rate changes on cash and cash equivalents	1	(7)
Net (decrease) increase in cash and cash equivalents	(36,250)	19,876
Cash and cash equivalents, beginning of period	112,292	59,215
Cash and cash equivalents, end of period	\$76,042	\$79,091
Supplemental disclosure of cash flow information		
Non-cash operating, investing, and financing activities		
Repurchase of common stock incurred but not yet paid	\$1,152	\$—
Property, plant, and equipment expenditures incurred but not yet paid	\$607	\$3,159
The accompanying notes are an integral part of these financial statements.		



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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements  
(unaudited)

1. Description of the Company and Basis of Presentation

The terms “Company” and “Vera Bradley” refer to Vera Bradley, Inc. and its subsidiaries, except where the context requires otherwise or where otherwise indicated.

Vera Bradley is a leading designer of women’s handbags and accessories, luggage and travel items, eyewear, and stationery and gifts. Founded in 1982 by friends Barbara Bradley Baekgaard and Patricia R. Miller, the brand’s iconic designs and versatile styles offer women of all ages a colorful way to accessorize every look.

Vera Bradley offers a unique, multi-channel sales model, as well as a focus on service and a high level of customer engagement. The Company sells its products through two reportable segments: Direct and Indirect. The Direct business consists of sales of Vera Bradley products through the Company’s full-line and factory outlet stores in the United States, verabradley.com, direct-to-consumer eBay sales, and the Company’s annual outlet sale in Fort Wayne, Indiana. As of August 1, 2015, the Company operated 107 full-line stores and 37 factory outlet stores. The Indirect business consists of sales of Vera Bradley products to approximately 2,700 specialty retail locations, substantially all of which are located in the United States, as well as department stores, national accounts, third-party e-commerce sites, the Company’s wholesale business in Japan, and third-party inventory liquidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”). Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) have been omitted. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Company’s Annual Report on Form 10-K for the fiscal year ended January 31, 2015, filed with the SEC.

The interim financial statements reflect all adjustments that are, in the opinion of management, necessary to present fairly the results for the interim periods presented. All such adjustments are of a normal, recurring nature. The results of operations for the thirteen and twenty-six weeks ended August 1, 2015, are not necessarily indicative of the results to be expected for the full fiscal year.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. The Company has eliminated intercompany balances and transactions in consolidation.

Fiscal Periods

The Company’s fiscal year ends on the Saturday closest to January 31. References to the fiscal quarters ended August 1, 2015, and August 2, 2014, refer to the thirteen-week periods ended on those dates.

Operating Leases and Tenant-Improvement Allowances

The Company has leases that contain rent holidays and predetermined, fixed escalations of minimum rentals. For each of these leases, the Company recognizes the related rent expense on a straight-line basis commencing on the date of initial possession of the leased property. The Company records the difference between the recognized rent expense and the amount payable under the lease as a deferred rent liability. As of August 1, 2015 and January 31, 2015, deferred rent liability was \$10.4 million and \$8.9 million, respectively, and is included within other long-term liabilities on the Consolidated Balance Sheets.

The Company receives tenant-improvement allowances from some of the landlords of its leased properties. These allowances generally are in the form of cash received by the Company from its landlords as part of the negotiated lease terms. The Company records each tenant-improvement allowance as a deferred credit and amortizes the allowance on a straight-line basis as a reduction to rent expense over the term of the lease, commencing on the possession date. As of August 1, 2015 and January 31, 2015, the deferred lease credit liability was \$16.7 million and

\$13.8 million, respectively. Of these amounts, \$2.2 million and \$1.8 million is included within other accrued liabilities as of August 1, 2015 and January 31, 2015, respectively; and \$14.5 million and \$12.0 million is included within other long-term liabilities as of August 1, 2015 and January 31, 2015, respectively.

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Vera Bradley, Inc.  
Notes to the Consolidated Financial Statements  
(unaudited)

Recently Issued Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. This guidance states that the disposal of a component of an entity is to be reported in discontinued operations only if the disposal represents a strategic shift that has (or will have) a major effect on an entity’s operations and financial results. The pronouncement also requires additional disclosures regarding individually significant disposals of components that do not meet the criteria to be recognized as a discontinued operation as well as additional and expanded disclosures. The guidance is effective for all disposals (or classifications as held for sale) of components of an entity and all businesses or nonprofit activities that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015; it is applied prospectively. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. The adoption of this standard did not have a material impact on the Company's Consolidated Financial Statements upon adoption.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This guidance requires companies to recognize revenue in a manner that depicts the transfer of promised goods or services to customers in amounts that reflect the consideration to which a company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The standard allows for either a full retrospective or a modified retrospective transition method. In August 2015, the FASB issued ASU 2015-14 to defer the effective date of ASU 2014-09 for all entities by one year to annual periods beginning after December 15, 2017, including interim periods within that reporting period, which for the Company is fiscal 2019. Earlier application is permitted as of the original effective date, annual reporting periods beginning after December 2016, including interim periods within that reporting period. The Company is currently evaluating the impact of this standard, including the transition method, on its consolidated results of operations, financial position and cash flows.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern which requires management to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and provide related footnote disclosures. The guidance is effective for annual or interim reporting periods beginning on or after December 15, 2016. Early adoption is permitted for financial statements that have not been previously issued. The standard allows for either a full retrospective or modified retrospective transition method. The Company does not expect this standard to have an impact on the Company’s Consolidated Financial Statements upon adoption.

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which modifies the presentation of debt issuance costs in financial statements. Under this new guidance, the Company will be required to present these costs in our condensed consolidated balance sheets as a direct deduction from the related debt liability. The requirements of the new standard will become effective for fiscal years, and interim periods within those fiscal years (including retrospective application), beginning after December 15, 2015; early adoption is permitted. The Company is currently evaluating this guidance and does not expect the application of this standard to have a material impact on the Company’s Consolidated Financial Statements upon adoption.

In July 2015, the FASB issued ASU 2015-11, Inventory, which requires entities to measure inventory at the lower of cost and net realizable value. This guidance is effective for interim and annual periods beginning on or after December 15, 2016. The Company is currently evaluating this guidance and does not expect the application of this standard to have a material impact on the Company’s Consolidated Financial Statements upon adoption.



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Vera Bradley, Inc.  
Notes to the Consolidated Financial Statements  
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## 2. Earnings Per Share

Basic earnings per share is computed based on the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed based on the weighted-average number of common shares outstanding, plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares represent outstanding restricted stock units. The components of basic and diluted earnings per share were as follows (in thousands, except per share data):

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Numerator:				
Income from continuing operations	\$5,715	\$7,894	\$1,579	\$14,771
Loss from discontinued operations, net of taxes	—	(296)	—	(606)
Net income	\$5,715	\$7,598	\$1,579	\$14,165
Denominator:				
Weighted-average number of common shares (basic)	39,315	40,686	39,600	40,663
Dilutive effect of stock-based awards	13	33	6	59
Weighted-average number of common shares (diluted)	39,328	40,719	39,606	40,722
Earnings per share - basic:				
Continuing operations	\$0.15	\$0.19	\$0.04	\$0.36
Discontinued operations	—	(0.01)	—	(0.01)
Net income	\$0.15	\$0.19	\$0.04	\$0.35
Earnings per share - diluted:				
Continuing operations	\$0.15	\$0.19	\$0.04	\$0.36
Discontinued operations	—	(0.01)	—	(0.01)
Net income	\$0.15	\$0.19	\$0.04	\$0.35

As of August 1, 2015 and August 2, 2014, there were an immaterial number of additional shares issuable upon the vesting of restricted stock units that were excluded from the diluted share calculations because they were anti-dilutive.

## 3. Fair Value of Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Assets and liabilities measured at fair value are classified using the following hierarchy, which is based upon the transparency of inputs to the valuation as of the measurement date:

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

Level 2 – Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly;

Level 3 – Unobservable inputs based on the Company's own assumptions.

The classification of fair value measurements within the hierarchy is based upon the lowest level of input that is significant to the measurement.

The carrying amounts reflected on the Consolidated Balance Sheets for cash and cash equivalents, receivables, other current assets, and payables as of August 1, 2015, and January 31, 2015, approximated their fair values.



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Notes to the Consolidated Financial Statements  
(unaudited)

4. Inventories

The components of inventories were as follows (in thousands):

	August 1, 2015	January 31, 2015
Raw materials <sup>(1)</sup>	\$1,203	\$5,542
Work in process	—	470
Finished goods	102,718	92,391
Total inventories	\$103,921	\$98,403

(1) The decrease in raw materials was primarily a result of the Company's finished goods suppliers purchasing and taking ownership of fabric.

5. Debt

As of August 1, 2015 and January 31, 2015, the Company had borrowing availability of \$125.0 million under its second amended and restated credit agreement.

6. Income Taxes

The provision for income taxes for interim periods is based on an estimate of the annual effective tax rate adjusted to reflect the impact of discrete items. Management judgment is required in projecting ordinary income to estimate the Company's annual effective tax rate.

The effective tax rate for the thirteen weeks ended August 1, 2015, was 39.3%, compared to 40.3% for the thirteen weeks ended August 2, 2014. The year-over year decrease is primarily due to the relative impact of discrete items occurring in the prior year but not the current year.

The effective tax rate for the twenty-six weeks ended August 1, 2015, was 63.8%, compared to 39.5% for the twenty-six weeks ended August 2, 2014. The year-over year increase is primarily due to the impact of discrete items, including an increase in income tax reserves for uncertain federal and state tax positions related to research and development tax credits from prior years.

7. Stock-Based Compensation

The Company recognizes share-based compensation expense, for its awards of restricted stock and restricted stock units, in an amount equal to the fair market value of the underlying stock on the grant date of the respective award. The Company reserved 6,076,001 shares of common stock for issuance or transfer under the 2010 Equity and Incentive Plan, which allows for grants of restricted stock units, as well as other equity awards.

Awards of Restricted Stock Units

During the thirteen weeks ended August 1, 2015, the Company granted 36,001 time-based and performance-based restricted stock units with an aggregate fair value of \$0.5 million to certain employees under the 2010 Equity and Incentive Plan compared to a total of 60,511 time-based and performance-based restricted stock units with an aggregate fair value of \$1.4 million granted in the same period of the prior year.

During the twenty-six weeks ended August 1, 2015, the Company granted 598,361 time-based and performance-based restricted stock units with an aggregate fair value of \$9.5 million to certain employees and non-employee directors under the 2010 Equity and Incentive Plan compared to a total of 278,491 time-based and performance-based restricted stock units with an aggregate fair value of \$7.3 million granted in the same period of the prior year. The Company determined the fair value of the awards based on the closing price of the Company's common stock on the grant date.

The majority of time-based restricted stock units vest and settle in shares of the Company's common stock, on a one-for-one basis, in equal installments on each of the first three anniversaries of the grant date. Beginning in fiscal 2014, all restricted stock units issued to non-employee directors vest after a one-year period from the grant date. The



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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements

(unaudited)

Company is recognizing the expense relating to these units, net of estimated forfeitures, on a straight-line basis over the vesting period.

Performance-based restricted stock units vest upon the completion of a three-year period of time (cliff vesting), subject to the employee's continuing employment throughout the three-year performance period and the Company's achievement of annual net income or earnings per share targets during the three-year performance period. The Company is recognizing the expense relating to these units, net of estimated forfeitures, based on the probable outcome of achievement of the financial targets, on a straight-line basis over three years.

The following table sets forth a summary of restricted stock unit activity for the twenty-six weeks ended August 1, 2015 (units in thousands):

	Time-based Restricted Stock Units		Performance-based Restricted Stock Units	
	Number of Units	Weighted- Average Grant Date Fair Value (per unit)	Number of Units	Weighted- Average Grant Date Fair Value (per unit)
Nonvested units outstanding at January 31, 2015	248	\$26.34	217	\$26.26
Granted	432	15.92	167	15.84
Vested	(118)	) 15.75	(8)	) 16.07
Forfeited	(64)	) 19.07	(60)	) 24.88
Nonvested units outstanding at August 1, 2015	498	\$20.75	316	\$21.26

As of August 1, 2015, there was \$8.9 million of total unrecognized compensation cost, net of estimated forfeitures, related to nonvested restricted stock units. That cost is expected to be recognized over a weighted-average period of 2.1 years.

## 8. Commitments and Contingencies

The Company is subject to various claims and contingencies arising in the normal course of business, including those relating to product liability, legal, employee benefit, environmental, and other matters. Management believes that it is not reasonably possible that any of these claims will have a material adverse effect on the Company's financial condition, results of operations, or cash flows.

## 9. Common Stock

On September 9, 2014, the Company's board of directors approved a share repurchase program (the "2014 Share Repurchase Program") authorizing up to \$40.0 million of repurchases of shares of the Company's common stock. The 2014 Share Repurchase Program expires in October 2016.

The Company purchased 1,574,380 shares at an average price of \$13.03 per share, excluding commissions, for an aggregate amount of \$20.5 million during the twenty-six weeks ended August 1, 2015. As of August 1, 2015, there was \$6.5 million remaining available to repurchase shares of the Company's common stock under the 2014 Share Repurchase Program. Subsequent to quarter end, the Company purchased 623,633 shares at an average price of \$10.47 per share, excluding commissions, which completed the 2014 Share Repurchase Program.

As of August 1, 2015, the Company held as treasury shares 2,195,365 shares of its common stock at an average price of \$15.25 per share, excluding commissions, for an aggregate carrying amount of \$33.5 million. The Company's

treasury shares may be issued under the 2010 Equity and Incentive Plan or for other corporate purposes.

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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements

(unaudited)

## 10. Discontinued Operations

On June 4, 2014, the Company entered into a five-year agreement with Mitsubishi Corporation Fashion Company and Look Inc. to import and distribute Vera Bradley products in Japan. As a result of moving to this wholesale business model, the Company exited its direct business in Japan during the third quarter of fiscal 2015 and the results of operations are reported as discontinued operations. Japan results were previously reported in the Direct segment, which has been restated to exclude the results of the discontinued operations for the periods presented. Following are the Japan results of operations (in thousands):

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Net revenues	\$—	\$1,144	\$—	\$2,408
Cost of sales	—	529	—	1,023
Gross profit	—	615	—	1,385
Selling, general, and administrative expenses	—	1,100	—	2,367
Operating loss	—	(485)	) —	(982)
Loss on disposal from discontinued operations	—	—	—	—
Loss before income taxes	—	(485)	) —	(982)
Income tax benefit	—	(189)	) —	(376)
Loss from discontinued operations	\$—	\$(296)	) \$—	\$(606)

## 11. Restructuring and Other Charges

In the first quarter of fiscal 2016, the Company closed its manufacturing facility located in New Haven, Indiana. The Company incurred restructuring and other charges during the first quarter of fiscal 2016 of approximately \$3.4 million (\$2.1 million after the associated tax benefit), related to the facility closing. These charges include severance and benefit costs of approximately \$1.7 million, lease termination costs of approximately \$0.7 million, inventory-related charges of approximately \$0.6 million, and other associated net costs, which include accelerated depreciation related to fixed assets, of approximately \$0.4 million. These charges are reflected in cost of sales in the Company's Consolidated Financial Statements. Management expects that the facility closure will reduce operating costs by approximately \$12.0 million annually beginning in the fourth quarter of fiscal 2016. All production from the facility will be absorbed by the Company's third party manufacturing suppliers.

A summary of charges and related liabilities, associated with the facility closure, are as follows (in thousands):

	Inventory-Related Charges	Lease Termination Costs	Severance and Benefits Costs	Other
Fiscal 2015 charges	\$ 2,989	\$—	\$—	\$7
Cash payments	—	—	—	—
Non-cash charges	(2,989)	) —	—	(7)
Liability as of January 31, 2015	\$ —	\$—	\$—	\$—
Fiscal 2016 charges	\$ 628	\$650	\$1,673	\$484
Cash payments	—	(650)	) (1,675)	) (198)
Non-cash charges	(628)	) —	2	(256)
Liability as of August 1, 2015	\$ —	\$—	\$—	\$30



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Vera Bradley, Inc.

Notes to the Consolidated Financial Statements

(unaudited)

Other charges affecting comparability of the financial results for the twenty-six weeks ended August 1, 2015 and August 2, 2014 totaled approximately \$3.1 million (\$2.1 million after the associated tax benefit) consisting of charges in the first quarter of fiscal 2016 of \$1.3 million in employee severance (reflected in selling, general, and administrative expenses), \$1.2 million due to a retail store early lease termination agreement (reflected in selling, general, and administrative expenses), and \$0.6 million related to an increase in income tax reserves for uncertain federal and state tax positions related to research and development tax credits (reflected in income tax expense).

**12. Segment Reporting**

The Company has two operating segments, which are also its reportable segments: Direct and Indirect. These operating segments are components of the Company for which separate financial information is available and for which operating results are evaluated on a regular basis by the chief operating decision maker in deciding how to allocate resources and in assessing the performance of the segments.

The Direct segment includes the Company's full-line and factory outlet stores, the Company's website, verabradley.com, direct-to-consumer eBay sales, and the annual outlet sale. Revenues generated through this segment are driven through the sale of Company-branded products from Vera Bradley to end consumers. The Company exited its direct Japan operations in the third quarter of fiscal 2015. Direct segment results for the current and prior periods presented are reported on a continuing operations basis unless otherwise stated. Discontinued operations are detailed in Note 10 Discontinued Operations of this Quarterly Report on Form 10-Q.

The Indirect segment represents revenues generated through the distribution of Company-branded products to specialty retailers representing approximately 2,700 locations, substantially all of which are located in the United States, as well as key accounts, which include department stores, national accounts, third-party e-commerce sites, the Company's wholesale business in Japan, and third-party inventory liquidation.

Corporate costs represent the Company's administrative expenses, which include, but are not limited to: human resources, legal, finance, information technology, design, merchandising, and various other corporate-level-activity-related expenses. All intercompany-related activities are eliminated in consolidation and are excluded from the segment reporting.

Company management evaluates segment operating results based on several indicators. The primary or key performance indicators for each segment are net revenues and operating income. Net revenues and operating income information for the Company's reportable segments during the thirteen and twenty-six weeks ended August 1, 2015 and August 2, 2014, respectively, consisted of the following (in thousands):

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Segment net revenues:				
Direct	\$83,775	\$77,777	\$154,208	\$149,961
Indirect	36,949	41,183	67,620	81,196
Total	\$120,724	\$118,960	\$221,828	\$231,157
Segment operating income:				
Direct	\$16,557	\$17,122	\$24,584	\$30,880
Indirect	14,788	15,947	24,692	31,386
Total	\$31,345	\$33,069	\$49,276	\$62,266
Reconciliation:				
Segment operating income	\$31,345	\$33,069	\$49,276	\$62,266
Less:				
Unallocated corporate expenses	(21,859)	) (19,823	) (44,761	) (37,733

Operating income	\$9,486	\$13,246	\$4,515	\$24,533
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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion summarizes the significant factors affecting the consolidated operating results, financial condition, liquidity, and cash flows of the Company as of and for the thirteen and twenty-six weeks ended August 1, 2015 and August 2, 2014. The following discussion should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended January 31, 2015, and our unaudited consolidated financial statements and the related notes included in Item 1 of this Quarterly Report.

Executive Summary

Below is a summary of our strategic progress and financial results for the second quarter of fiscal 2016 (all comparisons are to the second quarter of fiscal 2015):

Strategic Progress

We continued progressing product innovation by launching two new fabrications, our Wildwood leather and Preppy Poly collections.

We continued to increase the mix of higher-margin, made-for-outlet product in our factory outlet stores.

We continued to build a more flexible, efficient, and cost-effective supply chain through vendor and country diversification.

- We opened six new full-line stores and three new factory outlet stores during the second quarter.

We continued to make significant investments in marketing to modernize our brand and attract new customers.

We enhanced our e-commerce search capabilities.

Financial Summary

Net revenues increased 1.5% to \$120.7 million.

Direct segment sales increased 7.7% to \$83.8 million. Comparable sales (including e-commerce) decreased 15.0%.

Indirect segment sales decreased 10.3% to \$36.9 million.

Gross profit was \$66.6 million (55.1% of net revenue).

Operating income was \$9.5 million.

Income from continuing operations was \$9.4 million, or \$0.15 per diluted share.

Cash and cash equivalents were \$76.0 million at August 1, 2015.

Capital expenditures for the twenty-six weeks totaled \$15.4 million.

Repurchases of common stock for the thirteen weeks totaled \$13.3 million.

Discontinued Operations

In June 2014, we entered into a five-year agreement with Mitsubishi Corporation Fashion Company and Look Inc. to import and distribute Vera Bradley products in Japan. As a result of moving to this wholesale business model, we exited our direct business in Japan during the third quarter of fiscal 2015 and are accounting for it as a discontinued operation. Consolidated income statement and Direct segment results for the current and prior periods presented are reported on a continuing operations basis unless otherwise stated.

Restructuring and Other Charges Affecting Comparability of the Year-to-Date Periods ended August 1, 2015, and August 2, 2014

In the first quarter of fiscal 2016, the Company closed its manufacturing facility located in New Haven, Indiana. The Company incurred restructuring and other charges during the first quarter of fiscal 2016 of approximately \$3.4 million (\$2.1 million after the associated tax benefit), related to the facility closing. These charges include severance and benefit costs of approximately \$1.7 million, lease termination costs of approximately \$0.7 million, inventory-related charges of approximately \$0.6 million, and other associated net costs, which include accelerated depreciation related to fixed assets, of approximately \$0.4 million. These charges are reflected in cost of sales in the Company's Consolidated Financial Statements.

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Management expects that the facility closure will reduce operating costs by approximately \$12.0 million annually beginning in the fourth quarter of fiscal 2016. All production from the facility will be absorbed by the Company's third party manufacturing suppliers.

Other charges affecting comparability of the financial results for the twenty-six weeks ended August 1, 2015 and August 2, 2014 totaled approximately \$3.1 million (\$2.1 million after the associated tax benefit) consisting of charges in the first quarter of fiscal 2016 of \$1.3 million in employee severance (reflected in selling, general, and administrative expenses), \$1.2 million due to a retail store early lease termination agreement (reflected in selling, general, and administrative expenses), and \$0.6 million related to an increase in income tax reserves for uncertain federal and state tax positions related to research and development tax credits (reflected in income tax expense). See Note 11 to the Notes to the Consolidated Financial Statements, herein, for additional information.

### How We Assess the Performance of Our Business

In assessing the performance of our business, we consider a variety of performance and financial measures.

#### Net Revenues

Net revenues reflect sales of our merchandise and revenue from distribution and shipping and handling fees, less returns and discounts. Revenues for the Direct segment reflect sales through our full-line and factory outlet stores, verabradley.com, direct-to-consumer eBay sales, and our annual outlet sale in Fort Wayne, Indiana. Revenues for the Indirect segment reflect sales to specialty retail partners, department stores, national accounts, third-party e-commerce sites, our wholesale business in Japan, and third-party inventory liquidation.

#### Comparable Sales

Comparable sales (including e-commerce) are calculated based upon our stores that have been open for at least 12 full fiscal months and net revenues from our e-commerce operations. Comparable store sales are calculated based solely upon our stores that have been open for at least 12 full fiscal months. Remodeled stores are included in comparable sales and comparable store sales unless the store was closed for a portion of the current or comparable prior period or the remodel resulted in a significant change in square footage. Some of our competitors and other retailers calculate comparable or "same store" sales differently than we do. As a result, data in this report regarding our comparable sales and comparable store sales may not be comparable to similar data made available by other companies.

Non-comparable sales include sales from stores not included in comparable sales or comparable store sales.

Measuring the change in year-over-year comparable sales allows us to evaluate how our store base and e-commerce operations are performing. Various factors affect our comparable sales, including:

- Overall economic trends;
- Consumer preferences and fashion trends;
- Competition;
- The timing of our releases of new patterns and collections;
- Changes in our product mix;
- Pricing;
- The level of customer service that we provide in stores;
- Our ability to source and distribute products efficiently;
- The number of stores we open and close in any period; and
- The timing and success of promotional and advertising efforts.

#### Gross Profit

Gross profit is equal to our net revenues less our cost of sales. Cost of sales includes the direct cost of purchased and manufactured merchandise, distribution center costs, operations overhead, duty, and all inbound freight costs incurred. The components of our reported cost of sales may not be comparable to those of other retail and wholesale companies. Gross profit can be impacted by changes in volume; fluctuations in sales price; operational efficiencies, such as leveraging of fixed costs; promotional activities, such as free shipping; commodity prices, such as for cotton; and labor costs.



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Selling, General, and Administrative Expenses (SG&A)

SG&A expenses include selling; advertising, marketing, and product development; and administrative. Selling expenses include Direct business expenses, such as store expenses, employee compensation, and store occupancy and supply costs, as well as Indirect business expenses consisting primarily of employee compensation and other expenses associated with sales to Indirect retailers. Advertising, marketing, and product development expenses include employee compensation, media costs, creative production expenses, marketing agency fees, new product design costs, public relations expenses, and market research expenses. A portion of our advertising expenses may be reimbursed by Indirect retailers, and such amount is classified as other income. Administrative expenses include employee compensation for corporate functions, corporate headquarters occupancy costs, consulting and software expenses, and charitable donations.

Other Income

We support many of our Indirect retailers' marketing efforts by distributing certain catalogs and promotional mailers to current and prospective customers. Our Indirect retailers reimburse us for a portion of the cost to produce these materials. Reimbursement received is recorded as other income. The related cost to design, produce, and distribute the catalogs and mailers is recorded as SG&A expense. Other income also includes proceeds from the sales of tickets to our annual outlet sale.

Operating Income

Operating income is equal to gross profit less SG&A expenses plus other income. Operating income excludes interest income, interest expense, and income taxes.

Income from Continuing Operations

Income from continuing operations is equal to operating income less net interest expense and income taxes.

Loss from Discontinued Operations, Net of Taxes

Loss from discontinued operations, net of taxes, is equal to the loss from the results of operations related to the direct Japan business, which was exited in the third quarter of fiscal 2015, adjusted for the associated tax benefit.

Net Income

Net income is equal to the sum of income from continuing operations and loss from discontinued operations, net of taxes.

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## Results of Operations

The following tables summarize key components of our consolidated results of operations for the periods indicated, both in dollars and as a percentage of our net revenues (\$ in thousands):

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Statement of Income Data:				
Net revenues	\$120,724	\$118,960	\$221,828	\$231,157
Cost of sales	54,170	55,516	103,580	107,958
Gross profit	66,554	63,444	118,248	123,199
Selling, general, and administrative expenses	57,351	50,663	114,963	100,708
Other income	283	465	1,230	2,042
Operating income	9,486	13,246	4,515	24,533
Interest expense, net	72	24	149	104
Income from continuing operations before income taxes	9,414	13,222	4,366	24,429
Income tax expense	3,699	5,328	2,787	9,658
Income from continuing operations	5,715	7,894	1,579	14,771
Loss from discontinued operations, net of taxes	—	(296)	—	(606)
Net income	\$5,715	\$7,598	\$1,579	\$14,165
Percentage of Net Revenues:				
Net revenues	100.0	% 100.0	% 100.0	% 100.0
Cost of sales	44.9	% 46.7	% 46.7	% 46.7
Gross profit	55.1	% 53.3	% 53.3	% 53.3
Selling, general, and administrative expenses	47.5	% 42.6	% 51.8	% 43.6
Other income	0.2	% 0.4	% 0.6	% 0.9
Operating income	7.9	% 11.1	% 2.0	% 10.6
Interest expense, net	0.1	% —	% 0.1	% —
Income from continuing operations before income taxes	7.8	% 11.1	% 2.0	% 10.6
Income tax expense	3.1	% 4.5	% 1.3	% 4.2
Income from continuing operations	4.7	% 6.6	% 0.7	% 6.4
Loss from discontinued operations, net of taxes	—	% (0.2)	% —	% (0.3)
Net income	4.7	% 6.4	% 0.7	% 6.1

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The following tables present net revenues and operating income by operating segment, both in dollars and as a percentage of our net revenues, and store data for the periods indicated (\$ in thousands, except as otherwise indicated):

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Net Revenues by Segment:				
Direct	\$83,775	\$77,777	\$154,208	\$149,961
Indirect	36,949	41,183	67,620	81,196
Total	\$120,724	\$118,960	\$221,828	\$231,157
Percentage of Net Revenues by Segment:				
Direct	69.4	% 65.4	% 69.5	% 64.9
Indirect	30.6	% 34.6	% 30.5	% 35.1
Total	100.0	% 100.0	% 100.0	% 100.0
	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014	August 1, 2015	August 2, 2014
Operating Income by Segment:				
Direct	\$16,557	\$17,122	\$24,584	\$30,880
Indirect	14,788	15,947	24,692	31,386
Less: Corporate unallocated	(21,859 )	(19,823 )	(44,761 )	(37,733 )
Total	\$9,486	\$13,246	\$4,515	\$24,533
Operating Income as a Percentage of Net Revenues by Segment:				
Direct	19.8	% 22.0	% 15.9	% 20.6
Indirect	40.0	% 38.7	% 36.5	% 38.7
Store Data <sup>(1)</sup> :				
Total stores open at end of period	144	109	144	109
Comparable sales (including e-commerce) decrease <sup>(2)</sup>	(15.0 )%	(5.3 )%	(15.8 )%	(6.4 )%
Total gross square footage at end of period (all stores)	325,956	233,836	325,956	233,836
Average net revenues per gross square foot <sup>(3)</sup>	\$176	\$208	\$305	\$362

(1) Includes our full-line and factory outlet stores.

Comparable sales (including e-commerce) are calculated based upon our stores that have been open for at least 12 full fiscal months and net revenues from our e-commerce operations. Increase or decrease is reported as a

(2) percentage of the comparable sales for the same period in the prior fiscal year. Remodeled stores are included in comparable sales unless the store was closed for a portion of the current or comparable prior period or the remodel resulted in a significant change in square footage.

Dollars not in thousands. Average net revenues per gross square foot are calculated by dividing total net revenues

(3) for our stores that have been open at least 12 full fiscal months as of the end of the period by total gross square footage for those stores. Remodeled stores are included in average net revenues per gross square foot unless the store was closed for a portion of the period.

Thirteen Weeks Ended August 1, 2015, Compared to Thirteen Weeks Ended August 2, 2014

Net Revenues

For the thirteen weeks ended August 1, 2015, net revenues increased \$1.7 million, or 1.5%, to \$120.7 million, from \$119.0 million in the comparable prior-year period.

Direct. For the thirteen weeks ended August 1, 2015, net revenues in the Direct segment increased \$6.0 million, or 7.7%, to \$83.8 million, from \$77.8 million in the comparable prior-year period. This change resulted from a \$17.3 million increase in revenues at our non-comparable stores, which included 19 additional stores in the current year, partially offset by a comparable sales (including e-commerce) decrease of \$11.3 million, or 15.0%. The decrease in comparable sales (including e-commerce)

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includes a 14.7% decrease in e-commerce sales and 15.2% decrease in comparable store sales. The declines in comparable store sales and comparable sales (including e-commerce) were primarily due to year-over-year declines in store and e-commerce traffic, partially as a result of reduced promotional activity.

**Indirect.** For the thirteen weeks ended August 1, 2015, net revenues in the Indirect segment decreased \$4.3 million, or 10.3%, to \$36.9 million, from \$41.2 million in the comparable prior-year period. The decrease was primarily due to lower average order size from the Company's specialty retail accounts and a year-over-year reduction in the total number of specialty retail accounts, partially offset by the timing of the Company's summer product launch (which resulted in approximately \$3.7 million of revenues recognized in the second quarter of this year as compared to the first quarter of last year).

### **Gross Profit**

For the thirteen weeks ended August 1, 2015, gross profit increased \$3.2 million, or 4.9%, to \$66.6 million, from \$63.4 million in the comparable prior-year period. As a percentage of net revenues, gross profit increased to 55.1% for the thirteen weeks ended August 1, 2015, from 53.3% in the comparable prior-year period. The increase in gross profit as a percentage of net revenues was primarily due to the increased sales of higher-margin made-for-outlet product in the Company's factory outlet stores, leverage of overhead costs, Fall 2014 cost reductions at the Company's since-closed domestic manufacturing facility, lower levels of liquidation sales, and reduced promotional activity.

### **Selling, General, and Administrative Expenses**

For the thirteen weeks ended August 1, 2015, SG&A expenses increased \$6.7 million, or 13.2%, to \$57.4 million, from \$50.7 million in the comparable prior-year period. As a percentage of net revenues, SG&A expenses increased to 47.5% for the thirteen weeks ended August 1, 2015, from 42.6% in the comparable prior-year period. The \$6.7 million increase was primarily due to strategic investments which included incremental marketing, new store expenses, and e-commerce investments. SG&A expenses as a percentage of net revenues increased primarily due to the strategic investments, fixed expenses being spread over lower comparable revenues, as well as deleveraging of store operating expenses as a result of lower comparable store sales.

### **Other Income**

For the thirteen weeks ended August 1, 2015, other income decreased \$0.2 million, or 39.1%, to \$0.3 million, from \$0.5 million in the comparable prior-year period, primarily due to a decrease in reimbursement of co-op mailer expense from Indirect retailers.

### **Operating Income**

For the thirteen weeks ended August 1, 2015, operating income decreased \$3.7 million, or 28.4%, to \$9.5 million in the current year, from \$13.2 million in the comparable prior-year period. As a percentage of net revenues, operating income was 7.9% and 11.1% for the thirteen weeks ended August 1, 2015 and August 2, 2014, respectively. The decrease in operating income was due to an increase in selling, general, and administrative expenses and decrease in other income, partially offset by an increase in gross profit, which are described above.

**Direct.** For the thirteen weeks ended August 1, 2015, operating income in the Direct segment decreased \$0.5 million, or 3.3%, to \$16.6 million from \$17.1 million in the comparable prior-year period. As a percentage of Direct segment net revenues, operating income in the Direct segment was 19.8% and 22.0% for the thirteen weeks ended August 1, 2015 and August 2, 2014, respectively. The decrease in operating income was primarily due to strategic investments including new store expenses and e-commerce investments, partially offset by an increase in gross profit as a percentage of net revenues, which is described above.

**Indirect.** For the thirteen weeks ended August 1, 2015, operating income in the Indirect segment decreased \$1.1 million, or 7.3%, to \$14.8 million from \$15.9 million in the comparable prior-year period. As a percentage of Indirect segment net revenues, operating income in the Indirect segment was 40.0% and 38.7% for the thirteen weeks ended August 1, 2015 and August 2, 2014, respectively. The decrease in operating income is primarily due to a decrease in net revenues, partially offset by an increase in gross profit as a percentage of net revenues, which are described above.

**Corporate Unallocated.** For the thirteen weeks ended August 1, 2015, unallocated expenses increased \$2.1 million, or 10.3%, to \$21.9 million from \$19.8 million in the comparable prior-year period, primarily due to incremental marketing investments.

### **Income Tax Expense**

The effective tax rate for the thirteen weeks ended August 1, 2015, was 39.3%, compared to 40.3% for the thirteen weeks ended August 2, 2014. The year-over-year decrease is primarily due to the relative impact of discrete items occurring in the prior year but not the current year.

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### Income from Continuing Operations

For the thirteen weeks ended August 1, 2015, income from continuing operations decreased \$2.2 million, or 27.6%, to \$5.7 million from \$7.9 million in the comparable prior-year period.

### Loss from Discontinued Operations, Net of Taxes

For the thirteen weeks ended August 2, 2014, loss from discontinued operations, net of taxes, was \$0.3 million reflecting the Company's exit from Japan operations during the third quarter of fiscal 2015.

### Net Income

For the thirteen weeks ended August 1, 2015, net income decreased \$1.9 million, or 24.8%, to \$5.7 million from \$7.6 million in the comparable prior-year period.

### Twenty-Six Weeks Ended August 1, 2015, Compared to Twenty-Six Weeks Ended August 2, 2014

#### Net Revenues

For the twenty-six weeks ended August 1, 2015, net revenues decreased \$9.4 million, or 4.0%, to \$221.8 million, from \$231.2 million in the comparable prior-year period.

Direct. For the twenty-six weeks ended August 1, 2015, net revenues in the Direct segment increased \$4.2 million, or 2.8%, to \$154.2 million, from \$150.0 million in the comparable prior-year period. This change resulted from a \$26.7 million increase in revenues at our non-comparable stores, which included 19 additional stores in the current year, which was partially offset by a comparable sales (including e-commerce) decrease of \$21.7 million, or 15.8%. The decrease in comparable sales (including e-commerce) includes a 12.4% decrease in e-commerce sales, an 18.3% decrease in comparable store sales, as well as a decrease in total sales at our annual outlet sale compared to the prior year. The declines in comparable store sales and comparable sales (including e-commerce) were primarily due to year-over-year declines in store and e-commerce traffic, partially as a result of reduced promotional activity.

Indirect. For the twenty-six weeks ended August 1, 2015, net revenues in the Indirect segment decreased \$13.6 million, or 16.7%, to \$67.6 million, from \$81.2 million in the comparable prior-year period, primarily due to lower average order size from the Company's specialty retail accounts. In addition, there was a year-over-year reduction in the total number of specialty retail accounts.

#### Gross Profit

For the twenty-six weeks ended August 1, 2015, gross profit decreased \$5.0 million, or 4.0%, to \$118.2 million, from \$123.2 million in the comparable prior-year period. As a percentage of net revenues, gross profit was consistent at 53.3% for the twenty-six weeks ended August 1, 2015 and the comparable prior-year period. Gross profit included restructuring charges of \$3.4 million related to the closure of our manufacturing facility in the first quarter of fiscal 2016, as discussed in more detail in Note 11 to the Notes to the Consolidated Financial Statements herein, offset by increased sales of higher-margin made-for-outlet product in the Company's factory outlet stores, leverage of overhead costs, Fall 2014 cost reductions at the Company's since-closed domestic manufacturing facility, lower levels of liquidation sales, and reduced promotional activity.

#### Selling, General, and Administrative Expenses

For the twenty-six weeks ended August 1, 2015, SG&A expenses increased \$14.3 million, or 14.2%, to \$115.0 million, from \$100.7 million in the comparable prior-year period. As a percentage of net revenues, SG&A expenses increased to 51.8% for the twenty-six weeks ended August 1, 2015, from 43.6% in the comparable prior-year period. The increase in SG&A expenses for the twenty-six weeks ended August 1, 2015, included \$1.3 million in employee severance expense and \$1.2 million in expense related to a retail store early termination agreement that did not occur in the comparable period. The remaining increase was primarily due to strategic investments, which included incremental marketing, new store expenses, and e-commerce investments. SG&A expenses as a percentage of net revenues increased primarily due to the strategic investments, fixed expenses being spread over lower revenues and deleveraging of store operating expenses as a result of lower comparable store sales.

#### Other Income

For the twenty-six weeks ended August 1, 2015, other income decreased \$0.8 million, or 39.8%, to \$1.2 million, from \$2.0 million in the comparable prior-year period, primarily due to a decrease in reimbursement of co-op mailer expense from Indirect retailers.





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### Operating Income

For the twenty-six weeks ended August 1, 2015, operating income decreased \$20.0 million, or 81.6%, to \$4.5 million in the current year, from \$24.5 million in the comparable prior-year period. As a percentage of net revenues, operating income was 2.0% and 10.6% for the twenty-six weeks ended August 1, 2015 and August 2, 2014, respectively.

Operating income for the twenty-six weeks ended August 1, 2015, was negatively impacted by the \$5.9 million in restructuring and other charges described above under “Gross Profit” and “Selling, General, and Administrative Expenses.” The remaining decrease in operating income was due to an increase in selling, general, and administrative expenses and a decrease in other income and gross profit, which are described above.

Direct. For the twenty-six weeks ended August 1, 2015, operating income in the Direct segment decreased \$6.3 million, or 20.4%, to \$24.6 million from \$30.9 million in the comparable prior-year period. As a percentage of Direct segment net revenues, operating income in the Direct segment was 15.9% and 20.6% for the twenty-six weeks ended August 1, 2015 and August 2, 2014, respectively. Operating income in the Direct segment was negatively impacted by \$3.5 million in aggregate restructuring and other charges related to the closure of our manufacturing facility in the first quarter of fiscal 2016 and a retail store early termination agreement. The remaining decrease was primarily due to strategic investments including new store expenses and e-commerce investments, partially offset by an increase in gross profit as a percentage of net revenues, which is described above.

Indirect. For the twenty-six weeks ended August 1, 2015, operating income in the Indirect segment decreased \$6.7 million, or 21.3%, to \$24.7 million from \$31.4 million in the comparable prior-year period. As a percentage of Indirect segment net revenues, operating income in the Indirect segment was 36.5% and 38.7% for the twenty-six weeks ended August 1, 2015 and August 2, 2014, respectively. Operating income in the Indirect segment was negatively impacted by \$1.1 million in restructuring charges related to the closure of our manufacturing facility in the first quarter of fiscal 2016. The remaining decrease in operating income is primarily due to a decrease in net revenues, partially offset by an increase in gross profit as a percentage of net revenues, which are described above.

Corporate Unallocated. For the twenty-six weeks ended August 1, 2015, unallocated expenses increased \$7.1 million, or 18.6%, to \$44.8 million from \$37.7 million in the comparable prior-year period. The increase in unallocated expenses included \$1.3 million in employee severance expense. The remaining increase was primarily due to incremental marketing investments.

### Income Tax Expense

The effective tax rate for the twenty-six weeks ended August 1, 2015, was 63.8%, compared to 39.5% for the twenty-six weeks ended August 2, 2014. The year-over-year increase is primarily due to the impact of discrete items, including an increase in income tax reserves for uncertain federal and state tax positions related to research and development tax credits from prior years.

### Income from Continuing Operations

For the twenty-six weeks ended August 1, 2015, income from continuing operations decreased \$13.2 million, or 89.3%, to \$1.6 million from \$14.8 million in the comparable prior-year period. Included in this decrease were restructuring and other charges of \$6.5 million (\$4.2 million after the associated tax benefit), as described in Note 11 to the Notes to the Consolidated Financial Statements herein.

### Loss from Discontinued Operations, Net of Taxes

For the twenty-six weeks ended August 2, 2014, loss from discontinued operations, net of taxes was \$0.6 million reflecting the Japan operations which were exited during the third quarter of fiscal 2015.

### Net Income

For the twenty-six weeks ended August 1, 2015, net income decreased \$12.6 million, or 88.9%, to \$1.6 million from \$14.2 million in the comparable prior-year period. Included in this decrease were restructuring and other charges of \$6.5 million (\$4.2 million after the associated tax benefit), as described in Note 11 to the Consolidated Financial Statements herein.

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## Liquidity and Capital Resources

## General

Our primary source of liquidity is cash flow from operations. We also have access to additional liquidity, if needed, through borrowings under our \$125.0 million second amended and restated credit agreement. There were no borrowings under this agreement at August 1, 2015. Historically, our primary cash needs have been for merchandise inventories, payroll, store rent, capital expenditures associated with operational equipment, buildings, information technology, opening new stores, and debt repayments. The most significant components of our working capital are cash and cash equivalents, merchandise inventories, accounts receivable, accounts payable, and other current liabilities.

We believe that cash flows from operating activities and the availability of borrowings under our second amended and restated credit agreement or other financing arrangements will be sufficient to meet working capital requirements, anticipated capital expenditures, share repurchases, and debt payments for the foreseeable future.

## Cash Flow Analysis

A summary of operating, investing, and financing activities is shown in the following table (in thousands):

	Twenty-Six Weeks Ended	
	August 1, 2015	August 2, 2014
Net cash (used in) provided by operating activities	\$(998	) \$32,756
Net cash used in investing activities	(15,359	) (12,231 )
Net cash used in financing activities	(19,894	) (642 )
Net Cash (Used in) Provided by Operating Activities		

Net cash (used in) provided by operating activities consists primarily of net income adjusted for non-cash items, including depreciation, amortization, deferred taxes, and stock-based compensation, the effect of changes in assets and liabilities, and tenant-improvement allowances received from landlords under our store leases.

Net cash used in operating activities for the twenty-six weeks ended August 1, 2015, was \$1.0 million, compared to net cash provided by operating activities of \$32.8 million for the twenty-six weeks ended August 2, 2014. This decrease was primarily due to a decrease in net income of \$12.6 million along with a change in inventory balances that resulted in a \$5.5 million use of cash for the twenty-six weeks ended August 1, 2015, as compared to \$24.9 million of cash provided for the twenty-six weeks ended August 2, 2014.

## Net Cash Used in Investing Activities

Investing activities consist primarily of capital expenditures for growth related to new store openings, buildings, operational equipment, and information technology investments.

Net cash used in investing activities was \$15.4 million and \$12.2 million for the twenty-six weeks ended August 1, 2015 and August 2, 2014, respectively. The increase in capital expenditures was due primarily to the opening of 19 new stores in the first and second quarter of the current year as compared to ten stores in the comparable prior year period, which was partially offset by reduced spending for the campus consolidation project.

Capital expenditures for fiscal 2016 are expected to be approximately \$31.0 million.

## Net Cash Used in Financing Activities

Net cash used in financing activities was \$19.9 million for the twenty-six weeks ended August 1, 2015 which was primarily related to purchases of shares of the Company's common stock made under the 2014 Share Repurchase Program. This compares to net cash used in financing activities of \$0.6 million for the twenty-six weeks ended August 2, 2014.

## Second Amended and Restated Credit Agreement

On July 15, 2015, Vera Bradley Designs, Inc. ("VBD"), a wholly-owned subsidiary of the Company, entered into a Second Amended and Restated Credit Agreement among VBD, the lenders from time to time party thereto, JPMorgan Chase Bank, National Association, as administrative agent, Wells Fargo Bank, National Association, as syndication agent, and KeyBank National Association, as documentation agent (the "Credit Agreement"), which amended and restated our prior credit



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agreement. The Credit Agreement provides for certain credit facilities to VBD in an aggregate principal amount not to initially exceed \$125.0 million, the proceeds of which will be used for general corporate purposes of VBD and its subsidiaries, including but not limited to Vera Bradley International, LLC and Vera Bradley Sales, LLC (collectively, the “Named Subsidiaries”).

Amounts outstanding under the Credit Agreement bear interest, at VBD's option, at a per annum rate equal to either (A) the Alternate Base Rate (“ABR”) plus the Applicable Margin, where the ABR is the highest of (i) the prime rate, (ii) the federal funds rate plus 0.5%, and (iii) Adjusted LIBOR for a one-month interest period plus 1%, and the Applicable Margin is a percentage ranging from 0.00% to 0.70% depending upon the Company's leverage ratio or (B) Adjusted LIBOR plus the Applicable Margin, where Adjusted LIBOR means LIBOR, as adjusted for statutory reserve requirements for eurocurrency liabilities, and Applicable Margin is a percentage ranging from 1.00% to 1.70% depending upon the Company's leverage ratio. Any loans made, or letters of credit issued, pursuant to the Credit Agreement mature on July 15, 2020. As of August 1, 2015, the Company had borrowing availability of \$125.0 million under the agreement.

VBD's obligations under the Credit Agreement are guaranteed by the Company and the Named Subsidiaries. The obligations of VBD under the Credit Agreement are secured by first priority security interests in all of the respective assets of VBD, the Company, and the Named Subsidiaries and a pledge of the equity interests of VBD and the Named Subsidiaries.

The Credit Agreement contains various restrictive covenants, including restrictions on the Company's ability to dispose of assets, make acquisitions or investments, incur debt or liens, make distributions to stockholders or repurchase outstanding stock, enter into related party transactions and make capital expenditures, other than upon satisfaction of the conditions set forth in the Credit Agreement. The Company is also required to comply with certain financial and non-financial covenants, including maintaining a maximum leverage ratio, a minimum ratio of EBITDAR to the sum of interest expense plus rentals (as defined in the Credit Agreement), and a limit on capital expenditures. Upon an event of default, which includes certain customary events such as, among other things, a failure to make required payments when due, a failure to comply with covenants, certain bankruptcy and insolvency events, a material adverse change (as defined in the Credit Agreement), defaults under other material indebtedness, and a change in control, the lenders may accelerate amounts outstanding, terminate the agreement and foreclose on all collateral. The Company was in compliance with these covenants as of August 1, 2015.

### Off-Balance-Sheet Arrangements

We do not have any off-balance-sheet financing or unconsolidated special-purpose entities.

### Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, as well as the related disclosures of contingent assets and liabilities at the date of the financial statements. A summary of the Company's significant accounting policies is included in Note 2 to the Company's consolidated financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2015.

Certain accounting policies and estimates of the Company are considered critical, as these policies and estimates are the most important to the depiction of the Company's consolidated financial statements and require significant, difficult, or complex judgments, often about the effect of matters that are inherently uncertain. Such policies are summarized in the “Management's Discussion and Analysis of Financial Condition and Results of Operations” in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2015. As of August 1, 2015, there was no significant change to any of the critical accounting policies and estimates described in the Annual Report.

### Recently Issued Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. This guidance states that the disposal of a component of an entity is to be reported in discontinued operations only if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results. The pronouncement also requires additional disclosures regarding individually significant disposals of components that do

not meet the criteria to be recognized as a discontinued operation as well as additional and expanded disclosures. The guidance is effective for all disposals (or classifications as held for sale) of components of an entity and all businesses or nonprofit activities that, on acquisition, are classified as held for sale that occur within annual periods beginning on or after December 15, 2014, and interim periods within annual periods beginning on or after December 15, 2015; it is applied prospectively. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. The adoption of this standard did not have a material impact on the Company's Consolidated Financial Statements upon adoption.

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In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This guidance requires companies to recognize revenue in a manner that depicts the transfer of promised goods or services to customers in amounts that reflect the consideration to which a company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The standard allows for either a full retrospective or a modified retrospective transition method. In August 2015, the FASB issued ASU 2015-14 to defer the effective date of ASU 2014-09 for all entities by one year to annual periods beginning after December 15, 2017, including interim periods within that reporting period, which for the Company is fiscal 2019. Earlier application is permitted as of the original effective date, annual reporting periods beginning after December 2016, including interim periods within that reporting period. The Company is currently evaluating the impact of this standard, including the transition method, on its consolidated results of operations, financial position and cash flows.

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern which requires management to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and provide related footnote disclosures. The guidance is effective for annual or interim reporting periods beginning on or after December 15, 2016. Early adoption is permitted for financial statements that have not been previously issued. The standard allows for either a full retrospective or modified retrospective transition method. The Company does not expect this standard to have an impact on the Company's Consolidated Financial Statements upon adoption.

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which modifies the presentation of debt issuance costs in financial statements. Under this new guidance, the Company will be required to present these costs in our condensed consolidated balance sheets as a direct deduction from the related debt liability. The requirements of the new standard will become effective for fiscal years, and interim periods within those fiscal years (including retrospective application), beginning after December 15, 2015; early adoption is permitted. The Company is currently evaluating this guidance and does not expect the application of this standard to have a material impact on the Company's Consolidated Financial Statements upon adoption.

In July 2015, the FASB issued ASU 2015-11, Inventory, which requires entities to measure inventory at the lower of cost and net realizable value. This guidance is effective for interim and annual periods beginning on or after December 15, 2016. The Company is currently evaluating this guidance and does not expect the application of this standard to have a material impact on the Company's Consolidated Financial Statements upon adoption.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of August 1, 2015, there was no material change in the market risks described in “Quantitative and Qualitative Disclosures About Market Risks” in the Company’s Annual Report on Form 10-K for the fiscal year ended January 31, 2015.

ITEM 4. CONTROLS AND PROCEDURES

At the end of the period covered by this Quarterly Report on Form 10-Q, the Company carried out an evaluation, under the supervision and with the participation of the Company’s Disclosure Committee and management, including the Chief Executive Officer and the Chief Financial Officer of the effectiveness of the design and operation of the Company’s disclosure controls and procedures pursuant to Rule 13a-15 of the Securities Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures were effective as of August 1, 2015.

There has been no change in our internal control over financial reporting during the most recent fiscal quarter that has materially affected, or that is reasonably likely to materially affect, our internal control over financial reporting.

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## PART II. OTHER INFORMATION

## ITEM 1A. RISK FACTORS

There has been no material change to our risk factors as previously set forth in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2015.

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

On September 9, 2014, the Company's board of directors approved a share repurchase program (the "2014 Share Repurchase Program") authorizing up to \$40.0 million of repurchases of shares of the Company's common stock. The 2014 Share Repurchase Program expires in October 2016. During the thirteen weeks ended August 1, 2015, the Company repurchased 1,149,531 shares of the Company's common stock at an average price of \$11.60 per share, excluding commissions.

Details on the shares repurchased under the program during the thirteen weeks ended August 1, 2015 are as follows:

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 Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Program
May 3, 2015 - May 30, 2015	145,500	\$ 13.82	145,500	\$ 17,853,799
May 31, 2015 - July 4, 2015	460,000	11.51	460,000	12,560,534
July 5, 2015 - August 1, 2015	544,031	11.09	544,031	6,527,471
	1,149,531	\$ 11.60	1,149,531	



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ITEM 6. EXHIBITS

a. Exhibits

Exhibit No.	Description
10.1	Second Amended and Restated Credit Agreement dated as of July 15, 2015 among Vera Bradley Designs, Inc., JPMorgan Chase Bank, National Association, and the lenders party thereto
31.1	CEO Section 302 Certification
31.2	CFO Section 302 Certification
32.1	Section 906 Certifications*
101	The following materials from the Vera Bradley, Inc.'s Quarterly Report on Form 10-Q for the quarter ended August 1, 2015 formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Statements of Income for the Thirteen and Twenty-Six Weeks ended August 1, 2015 and August 2, 2014; (ii) Consolidated Statements of Comprehensive Income for the Thirteen and Twenty-Six Weeks ended August 1, 2015 and August 2, 2014; (iii) Consolidated Balance Sheets as of August 1, 2015 and January 31, 2015; (iv) Consolidated Statements of Cash Flows for the Twenty-Six Weeks ended August 1, 2015 and August 2, 2014, and (v) Notes to Consolidated Financial Statements. **

\* Furnished, not filed.

\*\* Pursuant to Rule 406T of SEC Regulation S-T, the Interactive Data Files included as 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 these Sections.

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SIGNATURE

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

Vera Bradley, Inc.  
(Registrant)

Date: September 9, 2015

/s/ Kevin J. Sierks  
Kevin J. Sierks  
Executive Vice President – Chief Financial Officer

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