STEVEN MADDEN, LTD.
Form 10-Q
November 09, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2016
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________________ to _____________________

Commission File Number 0-23702
STEVEN MADDEN, LTD.
(Exact name of registrant as specified in its charter)

Delaware	13-3588231
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

52-16 Barnett Avenue, Long Island City, New York	11104
(Address of principal executive offices)	(Zip Code)

(718) 446-1800
(Registrant's telephone number, including area code)

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

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 o

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

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (do not check if smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

As of November 8, 2016, the latest practicable date, there were 60,624,731 shares of the registrant's common stock, $0.0001 par value, outstanding.

STEVEN MADDEN, LTD.
FORM 10-Q
QUARTERLY REPORT
September 30, 2016

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STEVEN MADDEN, LTD. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(in thousands)

	September 30, 2016 (unaudited)	December 31, 2015	September 30, 2015 (unaudited)
ASSETS			
Current assets:			
Cash and cash equivalents	$ 62,723	$ 72,414	$ 38,654
Accounts receivable, net of allowances of $2,973, $2,306 and $2,589	39,507	43,173	23,269
Factor accounts receivable, net of allowances of $16,923, $21,756 and $21,977	230,346	155,211	261,566
Inventories	111,952	102,080	123,768
Marketable securities – available for sale	30,301	32,424	22,834
Prepaid expenses and other current assets	25,247	20,641	23,663
Prepaid taxes	5,606	17,484	—
Deferred taxes	14,573	14,392	14,302
Total current assets	520,255	457,819	508,056
Notes receivable	749	1,158	1,197
Note receivable – related party	2,730	2,990	3,074
Property and equipment, net	74,382	72,010	71,162
Deposits and other	4,896	5,088	5,422
Marketable securities – available for sale	90,436	88,465	89,705
Goodwill – net	136,522	137,097	143,589
Intangibles – net	146,398	149,758	147,680
Total Assets	$ 976,368	$ 914,385	$ 969,885
LIABILITIES			
Current liabilities:			
Accounts payable	$ 102,095	$ 79,790	$ 130,556
Accrued expenses	71,131	72,105	71,511
Income taxes payable	—	—	13,039
Contingent payment liability – current portion	16,682	16,763	19,893
Accrued incentive compensation	7,863	6,141	5,930
Total current liabilities	197,771	174,799	240,929
Contingent payment liability	—	8,012	13,286
Deferred rent	14,663	12,013	11,921
Deferred taxes	40,294	39,410	18,487
Other liabilities	—	1,488	—
Total Liabilities	252,728	235,722	284,623
Commitments, contingencies and other			
STOCKHOLDERS' EQUITY			
Preferred stock – $.0001 par value, 5,000 shares authorized; none issued; Series A Junior Participating preferred stock – $.0001 par value, 60 shares authorized; none issued	—	—	—
Common stock – $.0001 par value, 135,000 shares authorized, 86,109, 85,263 and 85,173 shares issued, 60,618, 61,693 and 62,564 shares outstanding	6	6	6

Additional paid-in capital	341,370	325,548	320,229
Retained earnings	989,003	896,842	871,109
Accumulated other comprehensive loss	(28,043)	(31,413)	(25,623)
Treasury stock – 25,491, 23,570, and 22,609 shares at cost	(578,973)	(512,579)	(480,834)
Total Steven Madden, Ltd. stockholders' equity	723,363	678,404	684,887
Noncontrolling interest	277	259	375
Total stockholders' equity	723,640	678,663	685,262
Total Liabilities and Stockholders' Equity	$ 976,368	$ 914,385	$ 969,885

See accompanying notes to condensed consolidated financial statements - unaudited.

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STEVEN MADDEN, LTD. AND SUBSIDIARIES
Condensed Consolidated Statements of Income
(unaudited)
(in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net sales	$408,384	$413,462	$1,063,143	$1,060,989
Cost of sales	253,876	264,691	671,388	684,694
Gross profit	154,508	148,771	391,755	376,295
Commission and licensing fee income – net	5,358	6,643	10,355	13,689
Operating expenses	(96,100)	(89,130)	(272,574)	(253,991)
Impairment charge	—	—	—	(3,045)
Income from operations	63,766	66,284	129,536	132,948
Interest and other income (expense) – net	747	(895)	1,117	273
Income before provision for income taxes	64,513	65,389	130,653	133,221
Provision for income taxes	20,810	22,298	38,212	45,428
Net income	43,703	43,091	92,441	87,793
Net (loss) income attributable to noncontrolling interest	(64)	206	278	578
Net income attributable to Steven Madden, Ltd.	$43,767	$42,885	$92,163	$87,215
Basic net income per share	$0.77	$0.73	$1.61	$1.47
Diluted net income per share	$0.74	$0.70	$1.54	$1.42
Basic weighted average common shares outstanding	56,869	58,911	57,334	59,271
Effect of dilutive securities – options/restricted stock	2,460	2,149	2,438	2,245
Diluted weighted average common shares outstanding	59,329	61,060	59,772	61,516

See accompanying notes to condensed consolidated financial statements - unaudited.

STEVEN MADDEN, LTD. AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income
(unaudited)
(in thousands)

	Three Months Ended September 30, 2016			Nine Months Ended September 30, 2016		
	Pre-tax amounts	Tax benefit/(expense)	After-tax amounts	Pre-tax amounts	Tax benefit/(expense)	After-tax amounts
Net income			$43,703			$92,441
Other comprehensive income (loss):						
Foreign currency translation adjustment	$(2,290)	$ —	(2,290)	$973	$ —	973
Gain or (loss) on cash flow hedging derivatives	447	(163)	284	688	(251)	437
Unrealized gain (loss) on marketable securities	543	(198)	345	3,087	(1,127)	1,960
Total other comprehensive income (loss)	$(1,300)	$ (361)	(1,661)	$4,748	$ (1,378)	3,370
Comprehensive income			42,042			95,811
Comprehensive (loss) income attributable to noncontrolling interests			(64)			278
Comprehensive income attributable to Steven Madden, Ltd.			$42,106			$95,533

	Three Months Ended September 30, 2015			Nine Months Ended September 30, 2015		
	Pre-tax amounts	Tax benefit/(expense)	After-tax amounts	Pre-tax amounts	Tax benefit/(expense)	After-tax amounts
Net income			$43,091			$87,793
Other comprehensive income (loss):						
Foreign currency translation adjustment	$(8,149)	$ —	(8,149)	$(12,644)	$ —	(12,644)
Gain or (loss) on cash flow hedging derivatives	940	(343)	597	400	(146)	254
Unrealized gain (loss) on marketable securities	(792)	289	(503)	(761)	278	(483)
Total other comprehensive income (loss)	$(8,001)	$ (54)	(8,055)	$(13,005)	$ 132	(12,873)
Comprehensive income			35,036			74,920
Comprehensive income attributable to noncontrolling interests			206			578
Comprehensive income attributable to Steven Madden, Ltd.			$34,830			$74,342

See accompanying notes to condensed consolidated financial statements - unaudited.

STEVEN MADDEN, LTD. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(unaudited)
(in thousands)

	Nine Months Ended September 30, 2016	2015
Cash flows from operating activities:		
Net income	$92,441	$87,793
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock-based compensation	14,618	13,609
Tax benefit from stock-based compensation	(3,846)	(10,428)
Depreciation and amortization	16,036	13,940
Loss on disposal of fixed assets	—	989
Impairment charges	—	3,045
Deferred taxes	(692)	(8,726)
Accrued interest on note receivable - related party	(48)	(52)
Deferred rent expense	2,650	348
Realized loss (gain) on sale of marketable securities	776	(82)
Changes in fair value on contingent liability	(45)	(2,504)
Changes, net of acquisitions, in:		
Accounts receivable	3,666	(12,718)
Factor accounts receivable	(75,135)	(77,523)
Notes receivable - related party	308	306
Inventories	(9,872)	(31,592)
Prepaid expenses, prepaid taxes, deposits and other	11,048	17,142
Accounts payable and accrued expenses	21,331	56,601
Accrued incentive compensation	1,722	—
Other liabilities	(1,488)	—
Net cash provided by operating activities	73,470	50,148
Cash flows from investing activities:		
Acquisitions, net of cash acquired	—	(9,129)
Capital expenditures	(12,908)	(13,524)
Purchases of marketable securities	(24,089)	(28,705)
Repayment of notes receivable	249	342
Maturity/sale of marketable securities	26,825	33,332
Net cash used in investing activities	(9,923)	(17,684)
Cash flows from financing activities:		
Proceeds from exercise of stock options	4,869	21,154
Purchase of noncontrolling interest	(3,665)	—
Tax benefit from the exercise of options	—	10,428
Payment of contingent liability	(8,048)	(2,950)
Common stock purchased for treasury	(66,394)	(103,892)
Net cash used in financing activities	(73,238)	(75,260)
Net (decrease) in cash and cash equivalents	(9,691)	(42,796)
Cash and cash equivalents – beginning of period	72,414	81,450

Cash and cash equivalents – end of period	$62,723	$38,654

See accompanying notes to condensed consolidated financial statements - unaudited.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2016
($ in thousands except share and per share data)

Note A – Basis of Reporting

The accompanying unaudited condensed consolidated financial statements of Steven Madden, Ltd. and subsidiaries (the "Company") have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP") for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, such statements include all adjustments (consisting only of normal recurring items) which are considered necessary for a fair presentation of the financial position of the Company and the results of its operations and cash flows for the periods presented. Certain adjustments were made to prior years' amounts to conform to the 2016 presentation. The results of operations for the three and nine month periods ended September 30, 2016 are not necessarily indicative of the operating results for the full year. These financial statements should be read in conjunction with the financial statements and related disclosures for the year ended December 31, 2015 included in the Annual Report of Steven Madden, Ltd. on Form 10-K filed with the SEC on February 26, 2016.

Note B – Use of Estimates

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

Significant areas involving management estimates include allowances for bad debts, returns and customer chargebacks, inventory valuation, valuation of intangible assets, litigation reserves and contingent payment liabilities. The Company provides reserves on trade accounts receivables and factor receivables for future customer chargebacks and markdown allowances, discounts, returns and other miscellaneous compliance-related deductions that relate to the current period sales. The Company evaluates anticipated chargebacks by reviewing several performance indicators of its major customers. These performance indicators, which include retailers' inventory levels, sell-through rates and gross margin levels, are analyzed by management to estimate the amount of the anticipated customer allowance.

Note C – Factor Receivable

The Company has a collection agency agreement with Rosenthal & Rosenthal, Inc. ("Rosenthal"). The agreement can be terminated by the Company or Rosenthal at any time upon 60 days prior written notice. Under the agreement, the Company can request advances from Rosenthal of up to 85% of aggregate receivables submitted to Rosenthal. The agreement provides the Company with a $30,000 credit facility with a $15,000 sub-limit for letters of credit at an interest rate based, at the Company's election, upon a calculation that utilizes either the prime rate minus 0.5% or LIBOR plus 2.5%. As of September 30, 2016 and 2015, no borrowings were outstanding. Further as of September 30, 2016 and 2015, there were open letters of credit of $0 and $337, respectively. The Company also pays Rosenthal a fee based on a percentage of the gross invoice amount submitted to Rosenthal. With respect to receivables related to our private label business, the fee is 0.14% of the gross invoice amount. With respect to all other receivables, the fee is 0.20% of the gross invoice amount. Rosenthal assumes the credit risk on a substantial portion of the receivables that the Company submits to it and, to the extent of any loans made to the Company, Rosenthal maintains a lien on the Company's receivables to secure the Company's obligations.

Note D – Notes Receivable

As of September 30, 2016 and December 31, 2015, Notes Receivable were comprised of the following:

	September 30, 2016	December 31, 2015
Note receivable from seller of SM Canada	$ 749	$ 1,158

In connection with the Company's February 21, 2012 acquisition of all of the assets comprising the footwear, handbags and accessories wholesale and retail businesses of Steve Madden Canada Inc., Steve Madden Retail Canada Inc., Pasa Agency Inc.

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STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2016
($ in thousands except share and per share data)

Note D – Notes Receivable (continued)

and Gelati Imports Inc. (collectively, "SM Canada"), which had been the Company's sole distributor in Canada since 1994, the Company provided an interest-free loan to the seller of SM Canada in the principal amount of $3,107 Canadian dollars (which converted to approximately $3,085 in U.S. dollars at the time of the acquisition). The note was recorded net of the imputed interest, which is being amortized to income over the term of the note. The loan is payable in five annual installments due on dates that correspond with the five annual earn-out payment dates under the acquisition agreement (to the extent such contingent consideration is earned as a result of SM Canada's financial performance in the earn-out periods; see Note F).

Any earn-out payment not achieved with respect to an earn-out period may result in less than the entire principal amount of the loan being repaid. In such event the unpaid annual installment of the principal amount of the loan will be forgiven.

Note E – Marketable Securities

Marketable securities consist primarily of certificates of deposit and corporate bonds with maturities greater than three months and up to ten years at the time of purchase as well as marketable equity securities. These securities, which are classified as available-for-sale, are carried at fair value, with unrealized gains and losses, net of any tax effect, reported in stockholders' equity as accumulated other comprehensive income (loss). These securities are classified as current and non-current marketable securities based upon their maturities. Amortization of premiums and discounts is included in interest income. For the three and nine months ended September 30, 2016, the amortization of bond premiums totaled $307 and $925 compared to $347 and $1,040 for the comparable period in 2015. The values of these securities may fluctuate as a result of changes in equity values, market interest rates and credit risk. The schedule of maturities at September 30, 2016 and December 31, 2015 are as follows:

	Maturities as of September 30, 2016		Maturities as of December 31, 2015	
	1 Year or Less	1 to 10 Years	1 Year or Less	1 to 10 Years
Corporate bonds	$11,628	$90,436	$11,240	$88,465
Certificates of deposit	18,673	—	21,184	—
Total	$30,301	$90,436	$32,424	$88,465

For the three and nine months ended September 30, 2016, gains of $3 and losses of $776 were reclassified from accumulated other comprehensive income and recognized in the income statement in other income compared to losses of $14 and gains of $82 for the comparable periods in 2015. For the nine month period ended September 30, 2016, current marketable securities included unrealized losses of $350 and long-term marketable securities included unrealized gains of $939 and unrealized losses of $35. For the comparable period in 2015, current marketable securities included unrealized losses of $640 while long-term marketable securities included unrealized gains of $151 and unrealized losses of $962.

Note F – Fair Value Measurement

The accounting guidance under Accounting Standards Codification "Fair Value Measurements and Disclosures" ("ASC 820-10") requires the Company to make disclosures about the fair value of certain of its assets and liabilities. ASC 820-10 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. ASC 820-10 utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. A brief description of those three levels is as follows:

- Level 1: Observable inputs such as quoted prices in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly.
- Level 3: Significant unobservable inputs.

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STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
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Note F – Fair Value Measurement (continued)

The Company's financial assets and liabilities subject to fair value measurements as of September 30, 2016 and December 31, 2015 are as follows:

		September 30, 2016 Fair Value Measurements		
	Fair value	Level 1	Level 2	Level 3
Assets:				
Cash equivalents	$3,308	$3,308	$—	$—
Current marketable securities – available for sale	30,301	30,301	—	—
Note receivable – related party	2,730	—	—	2,730
Note receivable from seller of SM Canada	749	—	—	749
Long-term marketable securities – available for sale	90,436	90,436	—	—
Forward contracts	160	—	160	—
Total assets	$127,684	$124,045	$160	$3,479
Liabilities:				
Contingent consideration	$16,682	$—	$—	$16,682
Total liabilities	$16,682	$—	$—	$16,682

		December 31, 2015 Fair Value Measurements		
	Fair value	Level 1	Level 2	Level 3
Assets:				
Cash equivalents	$2,242	$2,242	$ —	$—
Current marketable securities – available for sale	32,424	32,424	—	—
Note receivable – related party	2,990	—	—	2,990
Note receivable from seller of SM Canada	1,158	—	—	1,158
Long-term marketable securities – available for sale	88,465	88,465	—	—
Total assets	$127,279	$123,131	$ —	$4,148
Liabilities:				
Contingent consideration	$24,775	$—	$ —	$24,775
Total liabilities	$24,775	$—	$ —	$24,775

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STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
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Note F – Fair Value Measurement (continued)
The majority of our level 3 balances consist of contingent consideration related to various acquisitions and certain notes receivable. The changes in our level 3 assets and liabilities for the periods ended September 30, 2016 and December 31, 2015 are as follows:

2016	Balance at January 1,	Payments	Accrued Interest	Acquisitions	Change in estimate	Foreign Currency Translation	Balance at September 30,
Assets:							
Note receivable – related party	$2,990	(308)	48				$ 2,730
Note receivable – SM Canada	$1,158	(249)				(160)	$ 749
Liabilities:							
Contingent consideration	$24,775	(8,048)			(45)		$ 16,682

2015	Balance at January 1,	Payments	Accrued Interest	Acquisitions	Change in estimate	Foreign Currency Translation	Balance at December 31,
Assets:							
Note receivable – related party	$3,328	(409)	71				$ 2,990
Note receivable – SM Canada	$1,878	(466)				(254)	$ 1,158
Liabilities:							
Contingent consideration	$38,633	(6,270)			(5,576)	(2,012)	$ 24,775

Forward contracts are entered into to manage the risk associated with the volatility of future cash flows (see Note O). Fair value of these instruments is based on observable market transactions of spot and forward rates.
For the note receivable due from related party (see Note I) and due from the sellers of SM Canada (see Note D), the carrying value was determined to be the fair value, based upon their actual and imputed interest rates, which approximate current market interest rates.

The Company has recorded a liability for potential contingent consideration in connection with the December 30, 2014 acquisition of all of the outstanding capital stock of Trendy Imports S.A. de C.V., Comercial Diecisiette S.A. de C.V. and Maximus Designer Shoes S.A. de C.V. (together, "SM Mexico"). Pursuant to the terms of an earn-out agreement between the Company and the seller of SM Mexico, earn-out payments, if achieved, are due annually to the seller of SM Mexico based on the financial performance of SM Mexico for each of the twelve-month periods ending on December 31, 2015 and 2016, inclusive. The fair value of the contingent payments was estimated using the present value of management’s projections of the financial results of SM Mexico during the earn-out period. The current portion of the earn-out due, based on the twelve-month period ending December 31, 2015, approximates the recorded value. An earn-out payment of $3,483 for the period ended December 31, 2015 was paid to the seller of SM Mexico in the first quarter of this year.

The Company has recorded a liability for potential contingent consideration in connection with the August 13, 2014 acquisition of all of the outstanding capital stock of Dolce Vita Holdings, Inc. ("Dolce Vita"). Pursuant to the terms of an earn-out agreement between the Company and the seller of Dolce Vita, earn-out payments are due annually to the seller of Dolce Vita based on the financial performance of Dolce Vita for each of the twelve-month periods ending on September 30, 2015 and 2016, inclusive, provided that the aggregate minimum earn-out payment shall be no less than $5,000. The fair value of the contingent payments was estimated using the present value of management’s projections of the financial results of Dolce Vita during the earn-out period.

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
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Note F – Fair Value Measurement (continued)

The first earn-out payment of $1,019 was made to the sellers of Dolce Vita in the fourth quarter of 2015 and the second payment will be payable in the last quarter of 2016.

The Company has recorded a liability for potential contingent consideration in connection with the February 21, 2012 acquisition of SM Canada. Pursuant to the terms of an earn-out agreement between the Company and the seller of SM Canada, earn-out payments, if achieved, are due annually to the seller of SM Canada based on the financial performance of SM Canada for each of the 12-month periods ending on March 31, 2013 through 2017, inclusive. The fair value of the contingent payments was estimated using the present value of management's projections of the financial results of SM Canada during the earn-out period. An earn-out payment of $2,798 for the period ended March 31, 2016 was paid to the seller of SM Canada in the second quarter of this year.

The Company has recorded a liability for potential contingent consideration in connection with the May 25, 2011 acquisition of all of the outstanding shares of capital stock of Cejon, Inc. and Cejon Accessories, Inc. and all of the outstanding membership interests in New East Designs, LLC (collectively, "Cejon"). Pursuant to the terms of an earn-out agreement between the Company and the sellers of Cejon, earn-out payments, if achieved, are made annually to the sellers of Cejon, based on the financial performance of Cejon for each of the twelve-month periods ending on June 30, 2012 through 2016, inclusive. The fair value of the contingent payments was estimated using the present value of management's projections of the financial results of Cejon during the earn-out period. A final earn-out payment of $1,767 for the period ended June 30, 2016 was paid to the seller of Cejon, Inc. in the third quarter of this year.

The carrying value of certain financial instruments such as accounts receivable, factor accounts receivable and accounts payable approximates their fair values due to the short-term nature of their underlying terms. The fair values of investment in marketable securities available for sale are determined by reference to publicly quoted prices in an active market. Fair value of the notes receivable held by the Company approximates their carrying value based upon their imputed or actual interest rate, which approximates applicable current market interest rates.

Note G – Revenue Recognition

The Company recognizes revenue on wholesale sales when (i) products are shipped pursuant to its standard terms, which are freight on board Company warehouse, or when products are delivered to the consolidators, or any other destination, as per the terms of the customers' purchase order, (ii) persuasive evidence of an arrangement exists, (iii) the price is fixed and determinable and (iv) collection is reasonably assured. Sales reductions on wholesale sales for anticipated discounts, allowances and other deductions are recognized during the period when sales are recorded. With the exception of our cold weather accessories and Blondo businesses, normally we do not accept returns from our wholesale customers unless there are product quality issues, which we charge back to the vendors at cost. Sales of cold weather accessories and Blondo products to wholesale customers are recorded net of returns, which are estimated based on historical experience. Such amounts have historically not been material.

Retail sales are recognized when the payment is received from customers and are recorded net of estimated returns. The Company generates commission income acting as a buying agent by arranging to manufacture private label shoes to the specifications of its customers. The Company's commission revenue also includes fees charged for its design, product and development services provided to certain suppliers in connection with the Company's private label business. Commission revenue and product and development fees are recognized as earned when title to the product transfers from the manufacturer to the customer and collections are reasonably assured and are reported on a net basis after deducting related operating expenses.

The Company licenses its Steve Madden®, Steven by Steve Madden®, Madden Girl® and Stevies® trademarks for use in connection with the manufacture, marketing and sale of outerwear, hosiery, activewear, sleepwear, jewelry, watches, hair accessories, umbrellas, bedding, luggage, and men’s leather accessories. In addition, the Company licenses the Betsey Johnson® trademark for use in connection with the manufacture, marketing and sale of hosiery, swimwear, outerwear, sleepwear, activewear, jewelry, watches, bedding, luggage, stationery, umbrellas, and household goods; and furthermore, licenses the Dolce Vita® trademark for use in connection with the manufacture, marketing and sale of women's and children’s apparel. The license agreements require the licensee to pay the Company a royalty and, in substantially all of the agreements, an advertising fee, both of which are based on the higher of a minimum or a net sales percentage as defined in the various agreements. In addition, under

STEVEN MADDEN, LTD. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements – Unaudited
September 30, 2016
($ in thousands except share and per share data)

Note G – Revenue Recognition (continued)

the terms of retail selling agreements, most of the Company's international distributors are required to pay the Company a royalty based on a percentage of net retail sales, in addition to a commission and a design fee on the purchases of the Company's products. Licensing revenue is recognized on the basis of net sales reported by the licensees, or the minimum guaranteed royalties, if higher.

In substantially all of the Company's license agreements, the minimum guaranteed royalty is earned and receivable on a quarterly basis.

Note H – Sales Deductions

The Company supports retailers' initiatives to maximize sales of the Company's products on the retail floor by subsidizing the co-op advertising programs of such retailers, providing them with inventory markdown allowances and participating in various other marketing initiatives of its major customers. In addition, the Company accepts returns for damaged products for which the Company's costs are normally charged back to the responsible third-party factory. Such expenses are reflected in the condensed consolidated financial statements as deductions from gross sales to arrive at net sales.

Note I – Note Receivable – Related Party

On June 25, 2007, the Company made a loan to Steve Madden, its Creative and Design Chief and a principal stockholder of the Company, in the amount of $3,000 in order for Mr. Madden to satisfy a personal tax obligation resulting from the exercise of stock options that were due to expire and to retain the underlying Company common stock. Mr. Madden executed a secured promissory note in favor of the Company, for which a securities brokerage account maintained by Mr. Madden with his broker serves as collateral security. None of the securities held in the securities brokerage account are shares of the Company's common stock. There have been successive amendments of the secured promissory note, the most recent of which occurred on April 8, 2016, at which time the secured promissory note was amended to substitute the collateral securing the secured promissory note from shares of the Company's common stock to the security interest in Mr. Madden's securities brokerage account. Previously, on January 3, 2012, in connection with an amendment of Mr. Madden's employment contract, the secured promissory note was amended and restated to extend the maturity date of the obligation to December 31, 2023 and to eliminate the accrual of interest after December 31, 2011. Prior to its January 3, 2012 amendment and restatement, the secured promissory note was accruing interest at the rate of 6% per annum. In addition, the secured promissory note, as amended, provides that, commencing on December 31, 2014, and annually on each December 31 thereafter through the maturity date, one-tenth of the principal amount thereof, together with accrued interest, will be cancelled by the Company, provided that Mr. Madden continues to be employed by the Company on each such December 31. Contemporaneously, the Company will release its security interest in a portion of the securities held in Mr. Madden's securities brokerage account generally correlating to the amount of indebtedness cancelled on such date. As of December 31, 2011, $1,090 of interest has accrued on the principal amount of the loan evidenced by the secured promissory note related to the period prior to the elimination of the accrual of interest and has been reflected on the Company's Condensed Consolidated Financial Statements. Pursuant to the elimination of further interest accumulation under the secured promissory note, the outstanding principal amount of the loan and the accrued interest as of September 30, 2016 has been discounted to reflect imputed interest, which will be amortized over the remaining life of the loan. For the year ended December 31, 2015, the Company also recorded a charge in the amount of $409 to write-off the required one-tenth of the principal amount of the secured promissory note, which was partially offset by accrued imputed interest of $71.

Note J – Share Repurchase Program

The Company's Board of Directors authorized a share repurchase program (the “Share Repurchase Program”), effective as of January 1, 2004. The Share Repurchase Program does not have a fixed expiration or termination date and may be modified or terminated by the Board of Directors at any time. On several occasions the Board of Directors has increased the amount authorized for repurchase. The Share Repurchase Program permits the Company to effect repurchases from time to time through a combination of open market repurchases or in privately negotiated transactions at such prices and times as are determined to be in the best interest of the Company. On February 22, 2016, the Board of Directors approved the extension of the Share Repurchase Program
for an additional $136,000 in repurchases of the Company's common stock. During the nine months ended September 30, 2016, an aggregate of 1,700,088 shares of the Company's common stock were repurchased under the Share Repurchase Program, at an

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Note J – Share Repurchase Program (continued)

average price per share of $34.38, for an aggregate purchase price of approximately $58,445. As of September 30, 2016, approximately $134,126 remained available for future repurchases under the Share Repurchase Program.

Note K – Net Income Per Share of Common Stock

Basic net income per share is based on the weighted average number of shares of common stock outstanding during the period, which does not include unvested restricted common stock subject to forfeiture of 4,235,000 and 4,186,000 shares for the three and nine months ended September 30, 2016, respectively, compared to 4,037,000 and 4,058,000 shares for the three and nine months ended September 30, 2015. Diluted net income per share reflects: (a) the potential dilution assuming shares of common stock were issued upon the exercise of outstanding in-the-money options and the proceeds thereof were used to purchase shares of the Company's common stock at the average market price during the period, and (b) the vesting of granted non-vested restricted stock awards for which the assumed proceeds upon vesting are deemed to be the amount of compensation cost not yet recognized attributable to future services using the treasury stock method, to the extent dilutive. During the third quarter of 2016, the Company adopted Accounting Standards Update 2016-09 - Improvements to Employee Share-Based Payment Accounting, which provides updated guidance relating to the treasury stock calculation of diluted shares. (See Note R for further details.) For the three and nine months ended September 30, 2016, options to purchase approximately 383,000 and 375,000 shares of common stock, respectively, have been excluded in the calculation of diluted net income per share as compared to 6,000 and 15,000 shares that were excluded for the three and nine months ended September 30, 2015, as the result would have been antidilutive. For the three and nine months ended September 30, 2016 and 2015, all unvested restricted stock awards were dilutive.

Note L – Equity-Based Compensation

In March 2006, the Company's Board of Directors approved the Steven Madden, Ltd. 2006 Stock Incentive Plan (the "Plan") under which nonqualified stock options, stock appreciation rights, performance shares, restricted stock, other stock-based awards and performance-based cash awards may be granted to employees, consultants and non-employee directors. The stockholders approved the Plan on May 26, 2006. On May 25, 2007, the stockholders approved an amendment to the Plan to increase the maximum number of shares that may be issued under the Plan from 4,050,000 to 5,231,250. On May 22, 2009, the stockholders approved an amendment and restatement of the Plan that, among other things, increased the maximum number of shares that may be issued under the Plan to 13,716,000. On May 25, 2012, the stockholders approved an amendment to the Plan that increased the maximum number of shares that may be issued under the Plan to 23,466,000. The following table summarizes the number of shares of common stock authorized for use under the Plan, the number of stock-based awards granted (net of expired or cancelled awards) under the Plan and the number of shares of common stock available for the grant of stock-based awards under the Plan:

Common stock authorized	23,466,000
Stock-based awards, including restricted stock and stock options granted, net of expired or cancelled	(20,244,000)
Common stock available for grant of stock-based awards as of September 30, 2016	3,222,000

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Note L – Equity-Based Compensation (continued)

Total equity-based compensation for the three and nine months ended September 30, 2016 and 2015 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Restricted stock	$4,177	$3,792	$12,417	$11,120
Stock options	805	735	2,201	2,489
Total	$4,982	$4,527	$14,618	$13,609

Equity-based compensation is included in operating expenses on the Company's Condensed Consolidated Statements of Income.

Stock Options

Cash proceeds and intrinsic values related to total stock options exercised during the three and nine months ended September 30, 2016 and 2015 are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Proceeds from stock options exercised	$1,162	$1,451	$4,869	$21,154
Intrinsic value of stock options exercised	$634	$4,340	$11,684	$33,634

During the three and nine months ended September 30, 2016, options to purchase approximately 21,006 shares of common stock with a weighted average exercise price of $32.72 and options to purchase approximately 261,715 shares of common stock with a weighted average exercise price of $31.92 vested, respectively. During the three and nine months ended September 30, 2015, options to purchase approximately 23,074 shares of common stock with a weighted average exercise price of $31.02 and options to purchase approximately 416,275 shares of common stock with a weighted average exercise price of $26.94 vested, respectively. As of September 30, 2016, there were unvested options relating to 645,372 shares of common stock outstanding with a total of $4,024 of unrecognized compensation cost and an average vesting period of 1.60 years.

The Company uses the Black-Scholes option-pricing model to estimate the fair value of options granted, which requires several assumptions. The expected term of the options represents the estimated period of time until exercise and is based on the historical experience of similar awards. Expected volatility is based on the historical volatility of the Company's common stock. The risk
free interest rate is based on the U.S. Treasury yield curve in effect at the time of the grant. With the exception of special dividends paid in November of 2005 and 2006, the Company historically has not paid regular cash dividends and thus the expected dividend rate is assumed to be zero. The following weighted average assumptions were used for stock options granted during the nine months ended September 30, 2016 and 2015:

	2016	2015
Volatility	22.2% to 26.2%	22.4% to 28.3%
Risk free interest rate	0.86% to 1.73%	0.99% to 1.60%
Expected life in years	3.4 to 5.0	4.1 to 5.1
Dividend yield	0.00%	0.00%
Weighted average fair value	$7.01	$8.81

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Note L – Equity-Based Compensation (continued)

Activity relating to stock options granted under the Company's plans and outside the plans during the nine months ended September 30, 2016 is as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2016	2,016,000	$ 23.51		
Granted	249,000	33.73		
Exercised	(460,000)	10.59		
Cancelled/Forfeited	(30,000)	30.43		
Outstanding at September 30, 2016	1,775,000	$ 28.17	3.2 years	$ 11,329
Exercisable at September 30, 2016	1,128,000	$ 24.95	2.3 years	$ 10,836

Restricted Stock

The following table summarizes restricted stock activity during the nine months ended September 30, 2016 and 2015:

	2016		2015	
	Number of Shares	Weighted Average Fair Value at Grant Date	Number of Shares	Weighted Average Fair Value at Grant Date
Non-vested at January 1,	4,055,000	$ 25.32	4,067,000	$ 24.69
Granted	377,000	34.22	284,000	37.10
Vested	(193,000)	30.44	(235,000)	22.94
Forfeited	—	—	(68,000)	34.27
Non-vested at September 30,	4,239,000	$ 25.93	4,048,000	$ 25.29

As of September 30, 2016, the Company had $70,980 of total unrecognized compensation cost related to restricted stock awards granted under the Plan. This cost is expected to be recognized over a weighted average of 6.10 years. The Company determines the fair value of its restricted stock awards based on the market price of its common stock on the date of grant.

On January 3, 2012, the Company and its Creative and Design Chief, Steven Madden, entered into an amendment of Mr. Madden's existing employment agreement, pursuant to which, on February 8, 2012, Mr. Madden was granted 1,463,057 restricted shares of the Company's common stock at the then market price of $27.34, which will vest in equal annual installments over a seven-year period commencing on December 31, 2017 and, thereafter, on each December 31 through December 31, 2023, subject to Mr. Madden's continued employment on each such vesting date. On June 30, 2012, Mr. Madden exercised his right under his employment agreement to receive an additional restricted stock award, and, on July 3, 2012, he was granted 1,893,342 restricted shares of the Company's common stock at the then market price of $21.13, which will vest in the same manner as the aforementioned grant. On August 8, 2016, pursuant to the employment agreement, Mr. Madden was granted an option to purchase 150,000 shares of the Company's common stock at an exercise price of $34.42 per share, which option is exercisable in equal quarterly installments commencing on November 8, 2016.

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Note M – Acquisitions

Madlove, LLC

In June 2016, the Company paid $3,665 to acquire the remaining minority interest in Madlove, LLC ("Mad Love") thereby making Mad Love a wholly-owned subsidiary. Mad Love was formed as a joint venture in April 2011, in which the Company was the majority interest holder, had financial control and consolidated the financial statements of the joint venture. Mad Love designs and markets women's footwear under the Mad Love label. The Company has accounted for the acquisition of the minority interest as an equity transaction.

SM Europe

In April 2016, the Company formed a joint venture ("SM Europe") with SPM Shoetrade Holding B.V. through its subsidiary, Steve Madden Europe B.V. The Company is the majority interest holder in SM Europe and controls the joint venture. SM Europe is the exclusive distributor of the Company's products in Albania, Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Hungary, Ireland, Kosovo, Lithuania, Latvia, Luxembourg, the Netherlands, Norway, Poland, Romania, Russia, Slovakia, Slovenia, Sweden, Switzerland, and Tunisia. As the Company controls the joint venture and is the majority interest holder in SM Europe, the assets, liabilities and results of operations of SM Europe are included in the Company's Consolidated Financial Statements. The other member's interest is reflected in "Net income attributable to noncontrolling interests" in the Consolidated Statements of Income and "Noncontrolling interests" in the Consolidated Balance Sheets.

Note N – Goodwill and Intangible Assets

The following is a summary of the carrying amount of goodwill by segment as of September 30, 2016:

	Wholesale			Net
	Footwear	Accessories	Retail	Carrying Amount
Balance at January 1, 2016	$73,018	$ 49,324	$14,755	$137,097
Acquisitions	—	—	—	—
Purchase accounting adjustment	—	—	—	—
Translation and other	(289)	—	(286)	(575)
Balance at September 30, 2016	$72,729	$ 49,324	$14,469	$136,522

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Note N – Goodwill and Intangible Assets (continued)
The following table details identifiable intangible assets as of September 30, 2016:

	Estimated Lives	Cost Basis	Accumulated Amortization (1)	Impairment (2)	Net Carrying Amount
Trade names	6–10 years	$4,590	$ 3,232	$ —	$1,358
Customer relationships	10 years	41,509	20,351	—	21,158
License agreements	3–6 years	5,600	5,600	—	—
Non-compete agreement	5 years	2,440	2,402	—	38
Re-acquired right	2 years	4,200	3,954	—	246
Other	3 years	14	14	—	—
		58,353	35,553	—	22,800
Re-acquired right	indefinite	35,200	8,890	—	26,310
Trademarks	indefinite	100,333	—	3,045	97,288
		$193,886	$ 44,443	$ 3,045	$146,398

(1) Includes the effect of foreign currency translation related primarily to the movements of the Canadian dollar and Mexican peso in relation to the U.S. dollar.
(2) An impairment charge of $3,045 was recorded in the first quarter of 2015 related to the Company's Wild Pair trademark. The impairment was triggered by a loss of future anticipated cash flows from a significant customer.

The estimated future amortization expense of purchased intangibles as of September 30, 2016 is as follows:

2016 (remaining three months)	$1,342
2017	3,219
2018	3,088
2019	3,017
2020	2,232
Thereafter	9,902
	$22,800

Note O – Derivative Instruments

The Company uses derivative instruments, specifically, forward foreign exchange contracts, to manage the risk associated with the volatility of future cash flows. The foreign exchange contracts are used to mitigate the impact of exchange rate fluctuations on certain forecasted purchases of inventory and are designated as cash flow hedging instruments. As of September 30, 2016, the fair value of the Company's foreign currency derivatives, which is included on the Condensed Consolidated Balance Sheets in accrued expenses, is $160. As of September 30, 2016, $123 of gains related to cash flow hedges are recorded in accumulated other comprehensive loss, net of taxes and are expected to be recognized in earnings at the same time the hedged items affect earnings. As of September 30, 2015, $1,307 of losses related to cash flow hedges were recorded in accumulated other comprehensive loss, net of taxes. As of September 30, 2016, the Company's hedging activities were considered effective and, thus, no ineffectiveness from hedging activities were recognized in the Condensed Consolidated Statements of Income. For the three and nine months ended September 30, 2016, losses of $68 and $428 were reclassified from accumulated other comprehensive income and recognized in the income statement in cost of sales, as compared to losses of $671 and $1,396 for the three and nine months ended September 30, 2015.

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Note P – Commitments, Contingencies and Other
Legal proceedings:

Information regarding certain specific legal proceedings in which the Company is involved is contained in Part 1, Item 3, and in Note O to the notes to the Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015. Unless otherwise indicated in this report, all proceedings discussed in the earlier reports which are not indicated therein as having been concluded, remain outstanding as of September 30, 2016.

The Company has been named as a defendant in certain other lawsuits in the normal course of business. In the opinion of management, after consulting with legal counsel, the liabilities, if any, resulting from these matters should not have a material effect on the Company's financial position or results of operations. It is the policy of management to disclose the amount or range of reasonably possible losses in excess of recorded amounts.

Note Q – Operating Segment Information

The Company operates the following business segments: Wholesale Footwear, Wholesale Accessories, Retail, First Cost and Licensing. The Wholesale Footwear segment, through sales to department stores, mid-tier retailers, mass market merchants, online retailers and specialty stores, derives revenue, both domestically and worldwide (via our International business), from sales of branded and private label women’s, men’s, girls’ and children’s footwear. The Wholesale Accessories segment, which includes branded and private label handbags, belts and small leather goods as well as cold weather and selected other fashion accessories, derives revenue, both domestically and worldwide (via our International business), from sales to department stores, mid-tier retailers, mass market merchants, online retailers and specialty stores. Our Wholesale Footwear and Wholesale Accessories segments, through our International business, derive revenue from Albania, Austria, Belgium, Bulgaria, Canada, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Hungary, Ireland, Kosovo, Lithuania, Latvia, Luxembourg, Mexico, the Netherlands, Norway, Poland, Romania, Russia, Slovakia, Slovenia, Sweden, Switzerland, and Tunisia and, under special distribution arrangements in various other territories within Asia, Australia, Europe, the Middle East, India, South and Central America and New Zealand. The Retail segment, through the operation of Company-owned retail stores in the United States, Canada, Mexico and South Africa and the Company’s websites, derives revenue from sales of branded women’s, men’s and children’s footwear, accessories and licensed products to consumers. The First Cost segment represents activities of a subsidiary that earns commissions and design fees for serving as a buying agent of footwear products to mass-market merchandisers, mid-tier department stores and other retailers with respect to their purchase of footwear. In the Licensing segment, the Company generates revenue by licensing its Steve Madden®, Steven by Steve Madden®, Madden Girl® and Stevies® trademarks and other trademark rights for use in connection with the manufacture, marketing and sale of outerwear, hosiery, activewear, sleepwear, jewelry, watches, hair accessories, umbrellas, bedding, luggage, and men’s leather accessories. In addition, this segment licenses the Betsey Johnson® trademark for use in connection with the manufacture, marketing and sale of hosiery, swimwear, outerwear, sleepwear, activewear, jewelry, watches, bedding, luggage, stationery, umbrellas, and household goods; and furthermore, licenses the Dolce Vita® trademark for use in connection with the manufacture, marketing and sale of women's and children’s apparel.

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Note Q – Operating Segment Information (continued)

As of and for the three months ended,	Wholesale Footwear	Wholesale Accessories	Total Wholesale	Retail	First Cost	Licensing	Consolidated
September 30, 2016							
Net sales to external customers	$ 268,159	$ 78,448	$ 346,607	$ 61,777	$ —	$ —	$ 408,384
Gross profit	90,550	26,937	117,487	37,021	—	—	154,508
Commissions and licensing fees – net	—	—	—	—	2,424	2,934	5,358
Income from operations	38,195	17,931	56,126	2,282	2,424	2,934	63,766
Segment assets	$ 548,195	$ 209,329	757,524	168,378	50,466	—	976,368
Capital expenditures			$ 1,693	$ 2,800	$ —	$ —	$ 4,493
September 30, 2015							
Net sales to external customers	$ 276,446	$ 80,594	$ 357,040	$ 56,422	$ —	$ —	$ 413,462
Gross profit	86,774	27,909	114,683	34,088	—	—	148,771
Commissions and licensing fees – net	—	—	—	—	3,479	3,164	6,643
Income from operations	42,245	15,730	57,975	1,666	3,479	3,164	66,284
Segment assets	$ 556,238	$ 204,411	760,649	153,273	55,963	—	969,885
Capital expenditures			$ 1,329	$ 3,743	$ —	$ —	$ 5,072

As of and for the nine months ended,	Wholesale Footwear	Wholesale Accessories	Total Wholesale	Retail	First Cost	Licensing	Consolidated
September 30, 2016							
Net sales to external customers	$ 692,505	$ 192,769	$ 885,274	$ 177,869	$ —	$ —	$ 1,063,143
Gross profit	221,328	64,064	285,392	106,363			391,755
Commissions and licensing fees – net	—	—	—	—	3,929	6,426	10,355
Income from operations	83,132	31,745	114,877	4,304	3,929	6,426	129,536
Segment assets	$ 548,195	$ 209,329	757,524	168,378	50,466	—	976,368
Capital expenditures							