

Restoration Hardware Holdings Inc
Form 10-Q
June 17, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended May 4, 2013

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: 001-35720

RESTORATION HARDWARE HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

45-3052669
(I.R.S. Employer
Identification Number)

15 Koch Road, Suite J

Corte Madera, CA
(Address of principal executive offices)

94925
(Zip Code)

Registrant's telephone number, including area code: (415) 924-1005

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

As of June 10, 2013, 38,879,642 shares of registrant's common stock were outstanding.

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Table of Contents**PART I****Item 1. Financial Statements**

RESTORATION HARDWARE HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)

(Unaudited)

	May 4, 2013	February 2, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 9,669	\$ 8,354
Accounts receivable net	17,712	17,040
Merchandise inventories	365,716	353,329
Current deferred tax assets	37,006	37,006
Prepaid expense and other current assets	121,335	77,029
Total current assets	551,438	492,758
Property and equipment net	123,091	111,406
Goodwill	122,581	122,601
Trademarks and domain names	47,410	47,410
Other intangible assets net	2,134	2,713
Non-current deferred tax assets	6,868	6,873
Other assets	6,100	5,852
Total assets	\$ 859,622	\$ 789,613
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$ 179,420	\$ 145,353
Deferred revenue and customer deposits	43,095	41,643
Other current liabilities	32,666	32,428
Total current liabilities	255,181	219,424
Revolving line of credit	113,994	82,501
Deferred rent and lease incentives	30,867	30,784
Other long-term obligations	4,530	5,293
Total liabilities	404,572	338,002
Commitments and contingencies (See Note 12 to the unaudited Condensed Consolidated Financial Statements)		
Stockholders equity:		
Common stock, \$0.0001 par value per share, 180,000,000 shares authorized, 38,856,251 shares issued and 38,108,092 shares outstanding as of May 4, 2013 and 38,856,251 shares issued and 37,967,635 shares outstanding as of February 2, 2013	4	4
Additional paid-in capital	509,514	505,883
Accumulated other comprehensive income	1,180	1,211
Accumulated deficit	(55,648)	(55,487)

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Total stockholders' equity	455,050	451,611
Total liabilities and stockholders' equity	\$ 859,622	\$ 789,613

The accompanying notes are an integral part of these unaudited Condensed Consolidated Financial Statements.

Table of Contents**RESTORATION HARDWARE HOLDINGS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except share and per share amounts)****(Unaudited)**

	Three Months Ended	
	May 4, 2013	April 28, 2012
Net revenues	\$ 301,337	\$ 217,914
Cost of goods sold	199,460	142,646
Gross profit	101,877	75,268
Selling, general and administrative expenses	101,366	77,365
Income (loss) from operations	511	(2,097)
Interest expense	(840)	(1,575)
Loss before income taxes	(329)	(3,672)
Income tax expense (benefit)	(168)	56
Net loss	\$ (161)	\$ (3,728)
Weighted-average shares used in computing basic and diluted net loss per share	38,076,026	1,000
Basic and diluted net loss per share	\$	\$ (3,728)

The accompanying notes are an integral part of these unaudited Condensed Consolidated Financial Statements.

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RESTORATION HARDWARE HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(In thousands)

(Unaudited)

	Three Months Ended	
	May 4, 2013	April 28, 2012
Net loss	\$ (161)	\$ (3,728)
Foreign currency translation adjustment net of tax	(31)	43
Total comprehensive loss	\$ (192)	\$ (3,685)

The accompanying notes are an integral part of these unaudited Condensed Consolidated Financial Statements.

Table of Contents**RESTORATION HARDWARE HOLDINGS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

	Three Months Ended	
	May 4, 2013	April 28, 2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (161)	\$ (3,728)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	6,630	6,424
Stock-based compensation expense	3,631	387
Amortization of financing fees	168	147
Change in assets and liabilities:		
Accounts receivable	(672)	(5,831)
Merchandise inventories	(12,437)	(24,039)
Prepaid expense and other current assets	(44,307)	(13,233)
Other assets	(400)	216
Accounts payable and accrued expenses	25,978	20,815
Deferred revenue and customer deposits	1,452	7,120
Other current liabilities	339	(1,813)
Deferred rent and lease incentives	115	4,405
Other long-term obligations	41	163
Net cash used in operating activities	(19,623)	(8,967)
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(9,737)	(6,193)
Net cash used in investing activities	(9,737)	(6,193)
CASH FLOWS FROM FINANCING ACTIVITIES		
Gross borrowings under revolving line of credit	353,258	246,756
Gross repayments under revolving line of credit	(321,765)	(228,793)
Payments on capital leases	(840)	(1,110)
Net cash provided by financing activities	30,653	16,853
Effects of foreign currency exchange rate translation	22	
Net increase in cash and cash equivalents	1,315	1,693
Cash and cash equivalents		
Beginning of period	8,354	8,512
End of period	\$ 9,669	\$ 10,205
Non-cash transactions:		
Capital expenditures included in accounts payable at period end	\$ 8,107	\$ 1,915

The accompanying notes are an integral part of these unaudited Condensed Consolidated Financial Statements.

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RESTORATION HARDWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 THE COMPANY

Nature of Business

Restoration Hardware Holdings, Inc., a Delaware corporation, together with its subsidiaries (collectively, the Company), is a luxury home furnishings retailer that offers a growing number of categories including furniture, lighting, textiles, bathware, decorative accessories, outdoor and children's furnishings. These products are sold through the Company's stores, catalogs and websites. As of May 4, 2013, the Company operated a total of 70 retail stores and 14 outlet stores in 29 states, the District of Columbia and Canada, and had sourcing operations in Shanghai and Hong Kong.

The Company was formed on August 18, 2011 and capitalized on September 2, 2011 as a holding company for the purposes of facilitating an initial public offering of common equity and is a direct subsidiary of Home Holdings, LLC, a Delaware limited liability company (Home Holdings).

On November 1, 2012, the Company acquired all of the outstanding shares of capital stock of Restoration Hardware, Inc., a Delaware corporation, and Restoration Hardware, Inc. became a direct, wholly owned subsidiary of the Company. Restoration Hardware, Inc. was a direct, wholly owned subsidiary of Home Holdings prior to the Company's initial public offering. Outstanding units issued by Home Holdings under its equity compensation plan, referred to as the Team Resto Ownership Plan, were replaced with common stock of the Company at the time of its initial public offering. These transactions are referred to as the Reorganization. As a result of these transactions, as of November 1, 2012, 32,188,891 shares of the Company's common stock were outstanding.

On November 7, 2012, the Company completed its initial public offering. In connection with its initial public offering, the Company issued and sold 4,782,609 shares of its common stock at a price of \$24.00 per share. In addition, certain of the Company's stockholders sold an aggregate of 381,723 shares of common stock held by them in the initial public offering. Further, certain stockholders sold an additional aggregate of 774,650 shares of common stock held by them pursuant to the exercise by the offering's underwriters of their option to purchase additional shares. The Company did not receive any proceeds from the sale of stock by its stockholders.

Prior to the Reorganization, Restoration Hardware Holdings, Inc. had not engaged in any business or other activities except in connection with its formation and the Reorganization. Accordingly, all financial and other information herein relating to periods prior to the completion of the Reorganization is that of Restoration Hardware, Inc.

On May 20, 2013, the Company completed its follow-on offering of 9,974,985 shares of common stock at an offering price of \$50.00 per share, which included 1,301,085 shares sold in connection with the full exercise of the option to purchase additional shares granted to the underwriters. All of the shares sold in the offering were sold by existing stockholders of the Company. No shares were sold by the Company in the offering, and, as such, the Company did not receive any of the proceeds from such sales.

Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements have been prepared from the Company's records and, in management's opinion, include all adjustments (consisting of normal recurring adjustments) necessary to fairly state the Company's financial position as of May 4, 2013, and the results of operations and changes of cash flows for the three months ended May 4, 2013 and April 28, 2012, which each consist of thirteen weeks. The Company's current fiscal year ends on February 1, 2014 (fiscal 2013).

Certain information and disclosures normally included in the notes to annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted for purposes of these interim condensed consolidated financial statements.

These unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended February 2, 2013 (fiscal 2012).

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The results of operations for the three months ended May 4, 2013 presented herein are not necessarily indicative of the results to be expected for the full fiscal year.

Table of Contents**NOTE 2 CHANGE IN ACCOUNTING PRINCIPLE STOCK-BASED COMPENSATION**

In the third quarter of fiscal 2012, the Company changed its policy for recognizing stock-based compensation expense from the graded method of accounting to the straight-line method of accounting for its time-based units (or service-only awards). The Company previously disclosed this change in accounting policy and retrospectively restated its consolidated financial statements for such change in its audited consolidated financial statements for fiscal 2012.

Based on research and analysis, the Company believes the straight-line method of accounting for stock-based compensation expense for service-only awards is the predominant method used in its industry. In order for the Company's results of operations to be comparable to its peers, it has concluded that the straight-line method of accounting for stock-based compensation is a preferable accounting method in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 250-10-45.

The following table presents the unaudited comparative effect of the change in accounting method and its impact on key components of the Company's condensed consolidated statements of operations (*in thousands, except share and per share amounts*):

	Three Months Ended	
	April 28, 2012	
	Graded Method	Straight-Line Method
Net revenues	\$ 217,914	\$ 217,914
Cost of goods sold	142,646	142,646
Gross profit	75,268	75,268
Selling, general and administrative expense	77,401	77,365
Loss from operations	(2,133)	(2,097)
Interest expense	(1,575)	(1,575)
Loss before income taxes	(3,708)	(3,672)
Income tax expense	56	56
Net loss	\$ (3,764)	\$ (3,728)
Shares used in computing basic and diluted net loss per share	1,000	1,000
Basic and diluted net loss per share	\$ (3,764)	\$ (3,728)

NOTE 3 RECENT ACCOUNTING PRONOUNCEMENTS

The FASB is currently working on amendments to existing accounting standards governing a number of areas including, but not limited to, accounting for leases. In May 2013, the FASB issued a new exposure draft, *Leases* (the Exposure Draft), which would replace the existing guidance in ASC Topic 840, *Leases*. Under the Exposure Draft, among other changes in practice, a lessee's rights and obligations under most leases, including existing and new arrangements, would be recognized as assets and liabilities, respectively, on the balance sheet. Other significant provisions of the Exposure Draft include (i) defining the lease term to include the noncancellable period together with periods for which there is a significant economic incentive for the lessee to extend or not terminate the lease; (ii) defining the initial lease liability to be recorded on the balance sheet to contemplate only those variable lease payments that depend on an index or that are in substance fixed; and (iii) a dual approach for determining whether lease expense is recognized on a straight-line or accelerated basis, depending on whether the lessee is expected to consume more than an insignificant portion of the leased asset's economic benefits. The comment period for the Exposure Draft ends on September 13, 2013. If and when effective, this Exposure Draft will likely have a significant impact on the Company's consolidated financial statements. However, as the standard-setting process is still ongoing, the Company is unable to determine the impact this proposed change in accounting standards will have on its consolidated financial statements.

Table of Contents**NOTE 4 PREPAID EXPENSE AND OTHER CURRENT ASSETS**

Prepaid expense and other current assets consist of the following (*in thousands*):

	May 4, 2013	February 2, 2013
Prepaid catalog	\$ 83,202	\$ 43,828
Vendor deposits	22,256	20,383
Prepaid expense	14,139	11,479
Other current assets	1,738	1,339
Total prepaid expense and other current assets	\$ 121,335	\$ 77,029

NOTE 5 GOODWILL AND INTANGIBLE ASSETS

The following sets forth the goodwill and intangible assets as of May 4, 2013 (*dollar amounts in thousands*):

	Gross Carrying Amount	Accumulated Amortization	Foreign Currency Translation	Net Book Value	Useful Life
Intangible assets subject to amortization:					
Core technologies	\$ 6,580	\$ (6,470)	\$	\$ 110	5 years
Fair value of leases					
Fair market write-up	10,443	(8,466)	47	2,024	(2)
Fair market write-down	(2,591)	1,861		(730) ⁽¹⁾	(2)
Total intangible assets subject to amortization	14,432	(13,075)	47	1,404	
Intangible assets not subject to amortization:					
Goodwill	122,285		296	122,581	
Trademarks and domain names	47,410			47,410	
Total intangible assets	\$ 184,127	\$ (13,075)	\$ 343	\$ 171,395	

(1) The fair market write-down of leases is included in other long-term obligations on the condensed consolidated balance sheets.

(2) The fair value of each lease is amortized over the life of the respective lease. The longest lease for which a fair value adjustment was recorded has a termination date in January 2019.

The following sets forth the goodwill and intangible assets as of February 2, 2013 (*dollar amounts in thousands*):

	Gross Carrying Amount	Accumulated Amortization	Foreign Currency Translation	Net Book Value	Useful Life
Intangible assets subject to amortization:					
Core technologies	\$ 6,580	\$ (6,141)	\$	\$ 439	5 years
Fair value of leases					
Fair market write-up	10,737	(8,511)	48	2,274	(2)

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Fair market write-down	(2,591)	1,789	(802) ⁽¹⁾	(2)
Total intangible assets subject to amortization	14,726	(12,863)	48	1,911
Intangible assets not subject to amortization:				
Goodwill	122,285		316	122,601
Trademarks and domain names	47,410			47,410
Total intangible assets	\$ 184,421	\$ (12,863)	\$ 364	\$ 171,922

- (1) The fair market write-down of leases is included in other long-term obligations on the condensed consolidated balance sheets.
- (2) The fair value of each lease is amortized over the life of the respective lease. The longest lease for which a fair value adjustment was recorded has a termination date in January 2019.

Table of Contents**NOTE 6 ACCOUNTS PAYABLE AND ACCRUED EXPENSES**

Accounts payable and accrued expenses consist of the following (*in thousands*):

	May 4, 2013	February 2, 2013
Accounts payable	\$ 74,712	\$ 81,608
Accrued catalog costs	42,548	6,906
Accrued compensation	22,386	16,621
Accrued freight and duty	15,866	17,639
Accrued sales taxes	10,727	12,783
Accrued occupancy	5,869	5,842
Accrued professional fees	3,897	2,114
Other accrued expenses	3,415	1,840
Total accounts payable and accrued expenses	\$ 179,420	\$ 145,353

Accounts payable included negative cash balances due to outstanding checks of \$9.8 million and \$28.1 million as of May 4, 2013 and February 2, 2013, respectively.

NOTE 7 LINE OF CREDIT

As of May 4, 2013, \$114.0 million was outstanding under the revolving line of credit and the undrawn borrowing availability under the revolving line of credit was \$138.5 million. There were \$20.2 million and \$19.5 million in outstanding letters of credit as of May 4, 2013 and February 2, 2013, respectively.

Borrowings under the revolving line of credit are subject to interest, at the borrowers' option, at either the bank's reference rate or LIBOR (or the BA Rate or the Canadian Prime Rate, as such terms are defined in the credit agreement, for Canadian borrowings denominated in Canadian dollars or the United States Index Rate or LIBOR for Canadian borrowings denominated in United States dollars) plus an applicable margin rate, in each case. The weighted-average interest rate for the revolving line of credit was 2.74% as of May 4, 2013.

The credit agreement contains various restrictive covenants, including, among others, limitations on the ability to incur liens, make loans or other investments, incur additional debt, issue additional equity, merge or consolidate with or into another person, sell assets, pay dividends or make other distributions, or enter into transactions with affiliates, along with other restrictions and limitations typical to credit agreements of this type and size. As of May 4, 2013, the Company was in compliance with all covenants contained in the credit agreement.

NOTE 8 INCOME TAXES

The effective tax rate was 51.06% and (1.51)% for the three months ended May 4, 2013, and April 28, 2012, respectively. The increase in the effective tax rate for the three months ended May 4, 2013 was primarily due to no longer recording a U.S. valuation allowance against net deferred tax assets, as well as non-deductible stock-based compensation charges.

As of the end of fiscal year 2012, the Company's U.S. operations achieved a position of cumulative profits (adjusted for permanent differences) for the most recent three-year period. The Company concluded that this record of cumulative profitability in recent years, coupled with its business plan for profitability in future periods, provided assurance that its future tax benefits more likely than not would be realized. Accordingly, in the fourth quarter of fiscal 2012, the Company released all of its U.S. valuation allowance of \$57.2 million against net deferred tax assets.

As of May 4, 2013, the Company has retained a valuation allowance of \$0.3 million against deferred tax assets for its Shanghai operations.

As of both May 4, 2013 and February 2, 2013, \$1.8 million of the exposures related to unrecognized tax benefits would affect the effective tax rate if realized and are included in other long-term obligations on the condensed consolidated balance sheets. These amounts are primarily associated with foreign tax exposures that would, if realized, reduce the amount of net operating losses that would ultimately be utilized. As of

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May 4, 2013, \$0.3 million of the exposures related to unrecognized tax benefits are expected to decrease in the next 12 months due to the lapse of the statute of limitations.

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Adjustments required upon adoption of accounting for uncertainty in income taxes related to deferred tax asset accounts were offset by the related valuation allowance. Future changes to the Company's assessment of the realizability of those deferred tax assets will impact the effective tax rate. The Company accounts for interest and penalties related to exposures as a component of income tax expense. The Company has accrued \$0.5 million of interest expense associated with exposures as of May 4, 2013 and February 2, 2013.

NOTE 9 EARNINGS PER SHARE

For the three months ended May 4, 2013, options and restricted stock units of 8,246,577 and 41,713, respectively, were excluded from the calculation of diluted net loss per share because their inclusion would have been anti-dilutive due to the Company's net loss in the period. The Company did not have any anti-dilutive securities in the three months ended April 28, 2012 because all securities granted in that period were granted by Home Holdings.

The weighted-average number of shares for the three months ended April 28, 2012 is calculated by giving effect to the capitalization of Restoration Hardware Holdings, Inc. on September 2, 2011.

NOTE 10 STOCK-BASED COMPENSATION

The Company accounts for stock-based compensation in accordance with applicable guidance, which requires the Company to estimate the value of securities issued based upon an option-pricing model and recognize this estimated value as compensation expense over the vesting periods.

Team Resto Ownership Plan

Home Holdings established the Team Resto Ownership Plan in fiscal 2009. Awards under the Team Resto Ownership Plan were granted by the Home Holdings and were made up of the following:

Time-based units time-based units vested in annual installments, generally over a five-year graded vesting period.

Performance-based units performance-based units vested based on a return on equity investment to the Company's investors between either two times and three times such investment or three times and five times such investment.

All stock-based compensation expense associated with the grants of units by Home Holdings to the Company's directors, executive officers and employees was recorded by the Company.

On November 7, 2012, the Company completed its initial public offering and at the time of the initial public offering, outstanding units under the Team Resto Ownership Plan were replaced with common stock of the Company.

The Company did not record any stock-based compensation expense for these time-based units in the three months ended May 4, 2013. The Company recorded stock-based compensation expense for time-based units of \$0.4 million in the three months ended April 28, 2012, which is included in selling, general and administrative expenses on the condensed consolidated statements of operations. No stock-based compensation cost has been capitalized in the accompanying condensed consolidated financial statements.

The Company recognizes expense associated with performance-based units when it becomes probable that the performance condition will be met. Once it becomes probable that a participant will vest, the Company recognizes compensation expense equal to the number of shares which have vested multiplied by the fair value of the related shares measured at the grant date. No expense was recorded in either the three months ended May 4, 2013 or April 28, 2012 related to these performance-based units.

2012 Equity Replacement Plan

In connection with the Reorganization, the Board of Directors adopted the Restoration Hardware 2012 Equity Replacement Plan (the Replacement Plan), and outstanding units under the Team Resto Ownership Plan were replaced with vested and unvested shares of common stock under the Replacement Plan, in some cases subject to selling restrictions.

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A portion of the shares issued under the Replacement Plan are unvested restricted shares issued to Carlos Alberini, the Company's Chief Executive Officer, and Gary Friedman, who serves as the Company's Creator and Curator, in replacement of certain of their performance-based units granted under the Team Resto Ownership Plan. With respect to the 1,331,548 shares received by Mr. Alberini and Mr. Friedman in replacement of certain of their performance-based units, such shares begin to vest during the 36-month period following the initial public offering when the price of the Company's common stock reaches a 10-day average closing price per share of \$31.00 for at least 10 consecutive trading days, and such shares shall fully vest when the price of the Company's common stock reaches a 10-day average closing price per share of \$46.50 for at least 10 consecutive trading days (with proportional vesting in between). In addition, with respect to the 512,580 shares received by Mr. Alberini and Mr. Friedman in replacement of certain of their performance-based units, such shares begin to vest during the 36-month period following the initial public offering

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when the 10-day average closing price of the Company's common stock exceeds the initial public offering price of \$24.00 per share for at least 10 consecutive trading days, and such shares fully vest when the 10-day average closing price of the Company's common stock reaches a price per share of \$31.00 for at least 10 consecutive trading days (with proportional vesting in between) during the period.

In connection with Mr. Friedman's resignation and new role as the Creator and Curator, 1,185,511 shares of unvested stock he received in replacement of certain performance-based units will be marked to market every period until the required vesting criteria are met in accordance with ASC Topic 718.

During the three months ended May 4, 2013, 140,457 shares of the 1,331,548 shares received by Mr. Alberini and Mr. Friedman in replacement of certain of their performance-based units had vested in accordance with the performance objective as described above. The Company recorded a non-cash compensation charge of \$3.4 million related to these awards in the three months ended May 4, 2013 which is included in selling, general and administrative expenses on the condensed consolidated statements of operations.

In May 2013, the remaining 748,159 shares received by Mr. Alberini and Mr. Friedman in replacement of certain of their performance-based units had vested in accordance with the performance objective described above. The Company will record a non-cash compensation charge of \$26.5 million related to these awards in the second quarter of fiscal 2013. No additional compensation expense will be recorded in future periods related to these awards.

2012 Stock Option Plan and 2012 Stock Incentive Plan

As of May 4, 2013, 8,246,577 options were outstanding with a weighted-average exercise price of \$41.34 per share and 8,093,077 options were vested with a weighted-average exercise price of \$41.48 per share.

The aggregate intrinsic value of options outstanding, options vested or expected to vest, and options exercisable as of May 4, 2013 was \$24.9 million, \$24.9 million, and \$24.1 million, respectively. Stock options exercisable as of May 4, 2013 had a weighted-average remaining contractual life of 9.50 years.

As of May 4, 2013, the total unrecognized compensation expense related to unvested options was \$1.2 million, which is expected to be recognized on a straight-line basis over a weighted-average period of 3.76 years.

As of May 4, 2013, the Company had 41,713 unvested restricted stock unit awards with a weighted-average grant date fair value of \$36.69 per share. No restricted stock unit awards vested during the three months ended May 4, 2013. As of May 4, 2013, there was \$1.1 million of total unrecognized compensation expense related to unvested restricted stock unit awards which is expected to be recognized over a weighted-average period of 3.06 years.

The Company recorded stock-based compensation expense of \$0.2 million in the three months ended May 4, 2013 with respect to grants of stock options and restricted stock unit awards, which is included in selling, general and administrative expenses on the condensed consolidated statements of operations. No stock-based compensation cost has been capitalized in the accompanying condensed consolidated financial statements.

NOTE 11 RELATED PARTY TRANSACTIONS

The Company's former Chairman and Co-Chief Executive Officer, Gary Friedman, resigned from these positions and as a director of the Company effective as of October 20, 2012. In connection with such resignation, Mr. Friedman and the Company entered into an advisory services agreement that provides for Mr. Friedman to advise the Company in his role as the Creator and Curator with respect to product development, merchandising and other creative matters. The agreement has a five-year term and is renewable for an additional five-year period. In addition, in connection with the Company's initial public offering, Home Holdings has agreed to invest \$5 million, consisting of \$2.5 million in an initial tranche and up to \$2.5 million in one or more additional tranches, directly or indirectly, in Hierarchy, LLC (Hierarchy), a newly formed entity in which Mr. Friedman has a controlling interest. If requested by Home Holdings and agreed to by the Company, the Company may make these subsequent investments. The Company will have the right to acquire all or a portion of Home Holdings' interest in Hierarchy between the second and third anniversaries of the Company's initial public offering, at the greater of the then fair market value and the price paid by Home Holdings. As of May 4, 2013, the initial investment tranche of \$2.5 million had not been funded by Home Holdings.

In addition, Home Holdings has assigned to the Company its right of first offer and co-sale right over the sale by Mr. Friedman of his interests in Hierarchy, its right of first offer over the sale of Hierarchy or any of its lines of business and its preemptive rights on issuances of additional interests in Hierarchy. The agreements among Hierarchy, Home Holdings, Mr. Friedman and the Company contemplate that the Company will

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enter into an agreement to provide Hierarchy with back office, logistics, supply chain and administrative support, with pricing determined based on the fair market value of such services. Unless otherwise agreed by Home Holdings, for two years from the date of the Hierarchy operating agreement, Hierarchy's line of business will be limited to apparel and apparel related businesses. In addition, Hierarchy will be permanently prohibited from entering into lines of business in which the

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Company is engaged and certain lines of business in which the Company may become engaged (other than luggage, which Hierarchy may enter into after such two year period). Mr. Friedman is also a significant stockholder in the Company and will continue to advise the Board of Directors in an observer capacity, with the honorary title of Chairman Emeritus.

NOTE 12 COMMITMENTS AND CONTINGENCIES***Commitments***

The Company has no off balance sheet commitments as of May 4, 2013.

Contingencies

The Company is involved from time to time in various legal claims, actions and complaints arising in connection with its business. The outcome of matters in which the Company is involved cannot be determined at this time and the results cannot be predicted with certainty and could result in unexpected expenses and liability and could also materially adversely affect the Company's operations.

The Company reviews the need for any loss contingency reserves and establishes reserves when, in the opinion of management, it is probable that a matter would result in liability, and the amount of loss, if any, can be reasonably estimated. Generally, in view of the inherent difficulty of predicting the outcome of those matters, particularly in cases in which claimants seek substantial or indeterminate damages, it is not possible to determine whether a liability has been incurred or to reasonably estimate the ultimate or minimum amount of that liability until the case is close to resolution, in which case no reserve is established until that time.

NOTE 13 SEGMENT REPORTING

The Company defines an operating segment on the same basis that it uses to evaluate performance internally by the Chief Operating Decision Maker (CODM). The Company has determined that the Chief Executive Officer (or Co-Chief Executive Officers prior to Mr. Friedman's resignation from such position) was its CODM and there was one operating segment. Therefore, the Company reports as a single segment. This includes all sales channels accessed by the Company's customers, including sales through catalogs, sales through the Company's website and sales through the Company's stores.

The Company classifies its sales into furniture and non-furniture product lines. Furniture includes both indoor and outdoor furniture from the Company's business lines. Non-furniture includes lighting, textiles, accessories and home décor. Net revenues in each category were as follows (*in thousands*):

	Three Months Ended	
	May 4, 2013	April 28, 2012
Furniture	\$ 171,373	\$ 113,824
Non-furniture	129,964	104,090
Total net revenues	\$ 301,337	\$ 217,914

The Company is domiciled in the United States and operates stores in the United States and Canada. Revenues from Canadian operations, and the long-lived assets in Canada, are not material to the Company. Geographic revenues are determined based upon where service is rendered.

No single customer accounted for more than 10% of the Company's revenues in the three months ended May 4, 2013 or April 28, 2012.

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

The following discussion and analysis of the financial condition and results of our operations should be read together with the condensed consolidated financial statements and the related notes of Restoration Hardware Holdings, Inc. included in Item 1 of Part I of this Quarterly Report on Form 10-Q and with the audited consolidated financial statements and the related notes of Restoration Hardware Holdings, Inc. included in our most recent Form 10-K filed on April 29, 2013.

FORWARD-LOOKING STATEMENTS AND MARKET DATA

This quarterly report contains forward-looking statements that are subject to risks and uncertainties. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, 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, will, should, likely and other words and terms in connection with any discussion of the timing or nature of future operating or financial performance or other events.

Forward-looking statements are subject to risk and uncertainties that may cause actual results to differ materially from those that we expected. We derive many of our forward-looking statements from our operating budgets and forecasts, which are based upon many detailed assumptions. While we believe that our assumptions are reasonable, we caution that it is very difficult to predict the impact of known factors and it is impossible for us to anticipate all factors that could affect our actual results. Important factors that could cause actual results to differ materially from our expectations, or cautionary statements, are disclosed under the sections entitled Risk Factors in Part II of this quarterly report and in our most recent Form 10-K filed on April 29, 2013, Management's Discussion and Analysis of Financial Condition and Results of Operations, and elsewhere in this quarterly report. All forward-looking statements attributable to us, or persons acting on our behalf, are expressly qualified in their entirety by these cautionary statements, as well as other cautionary statements. You should evaluate all forward-looking statements made in this quarterly report in the context of these risks and uncertainties.

We cannot assure you that we will realize the results or developments we expect or anticipate or, even if substantially realized, that they will result in the consequences or affect us or our operations in the way we expect. The forward-looking statements included in this quarterly 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 otherwise required by law.

Overview

We are a leading luxury retailer in the home furnishings marketplace. Our collections of timeless, updated classics and reproductions are presented consistently across our sales channels in sophisticated and unique lifestyle settings that we believe are on par with world-class interior designers. We offer dominant merchandise assortments across a growing number of categories, including furniture, lighting, textiles, bathware, décor, outdoor and garden, tableware and children's furnishings. Our business is fully integrated across our multiple channels of distribution, consisting of our stores, catalogs and websites. We position our stores as showrooms for our brand, while our catalogs and websites act as virtual extensions of our stores. As of May 4, 2013, we operated a total of 70 retail stores, consisting of 62 Galleries, 5 Full Line Design Galleries and 3 Baby & Child Galleries, as well as 14 outlet stores throughout the United States and Canada.

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The following table sets forth our statements of operations and other financial and operating data.

On November 7, 2012, Restoration Hardware Holdings, Inc. completed an initial public offering and acquired all of the outstanding shares of capital stock of Restoration Hardware, Inc. Outstanding units under the Team Resto Ownership Plan were exchanged for common stock of Restoration Hardware Holdings, Inc. at the time of its initial public offering. These transactions are referred to as the Reorganization. Restoration Hardware Holdings, Inc. has not engaged in any business or other activities except in connection with its formation and the Reorganization. Accordingly, all financial and other information herein relating to periods prior to the completion of the Reorganization is that of Restoration Hardware, Inc.

	Three Months Ended	
	May 4, 2013	April 28, 2012
	(dollars in thousands, excluding per square foot store data)	
Statements of Operations:		
Net revenues	\$ 301,337	\$ 217,914
Cost of goods sold	199,460	142,646
Gross profit	101,877	75,268
Selling, general and administrative expenses	101,366	77,365
Income (loss) from operations	511	(2,097)
Interest expense	(840)	(1,575)
Loss before income taxes	(329)	(3,672)
Income tax expense (benefit)	(168)	56
Net loss	\$ (161)	\$ (3,728)
Other Financial and Operating Data:		
Growth in net revenues:		
Stores ⁽¹⁾	39%	16%
Direct	38%	20%
Total	38%	18%
Retail ⁽²⁾ :		
Comparable store sales change ⁽³⁾	41	