FOREST LABORATORIES INC
Form DEF 14A
June 29, 2007

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

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Amendment No.)

Filed by registrant [X]
Filed by a party other than the registrant [ ]
Check the appropriate box:
[ ] Preliminary proxy statement
[X] Definitive proxy statement
[ ] Definitive additional materials
[ ] Soliciting material pursuant to §240.14a-12

Forest Laboratories, Inc.
(Name of Registrant as Specified in its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of filing fee (Check the appropriate box):

[X] No fee required.
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2) Aggregate number of securities to which transaction applies:

3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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2) Form, Schedule or Registration Statement No.:

3) Filing party:

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FOREST LABORATORIES, INC.

NOTICE OF
2007 ANNUAL MEETING OF STOCKHOLDERS

The Annual Meeting of the Stockholders of Forest Laboratories, Inc. will be held on August 13, 2007 at 10:00 a.m., at JP Morgan Chase & Co. Corporate Headquarters, 277 Park Avenue, New York, New York. We are holding this meeting to:

1. Elect eight directors to serve until the next Annual Meeting of Stockholders and until their successors are duly elected and qualified (Proposal 1);

2. Adopt the 2007 Equity Incentive Plan (Proposal 2);

3. Ratify the appointment of BDO Seidman, LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2008 (Proposal 3); and

4. Transact such other business as may properly be brought before the meeting.

The record date for the Annual Meeting is June 21, 2007. Only Forest stockholders of record at the close of business on that date may vote at the meeting, or any adjournment of the meeting. A copy of the Annual Report for the fiscal year ended March 31, 2007 is being mailed with this Proxy Statement.

You are invited to attend the meeting. Whether or not you plan to attend the meeting, please vote by mail, by telephone, or on the Internet in order to be certain your shares are represented at the meeting.

By Order of the Board of Directors

WILLIAM J. CANDEE, III,
Secretary

June 29, 2007

New York, New York

FOREST LABORATORIES, INC.
909 THIRD AVENUE
NEW YORK, NEW YORK 10022

PROXY STATEMENT

This Proxy Statement contains information related to our Annual Meeting of Stockholders to be held on Monday, August 13, 2007, beginning at 10:00 a.m. at JP Morgan Chase & Co. Corporate Headquarters, 277 Park Avenue, New York, New York, and at any adjournments thereof. This Proxy Statement is being sent to stockholders on or about June 29, 2007. You should review this information together with our 2007 Annual Report to Stockholders, which accompanies this Proxy Statement.

Information about the Meeting

Q: Why did you send me this Proxy Statement?

A: We sent you this Proxy Statement and the enclosed proxy card because the Board of Directors (the Board) of Forest Laboratories, Inc. (we or Forest) is soliciting your proxy to vote at our 2007 Annual Meeting of Stockholders (the meeting) to be held on Monday, August 13, 2007, or any adjournments of the meeting. This Proxy Statement summarizes information that is intended to assist you in making an informed vote on the proposals described in the Proxy Statement.

Q: Who can vote at the Annual Meeting?

A: Only stockholders of record as of the close of business on June 21, 2007 are entitled to vote at the meeting. On that date, there were 320,040,471 shares of our Common Stock outstanding and entitled to vote.

Q: How many shares must be present to conduct the Annual Meeting?

A: We must have a "quorum" present in person or by proxy to hold the Annual Meeting. A quorum is a majority of the outstanding common shares entitled to vote. Abstentions and broker non-votes (defined below) will be counted for the purpose of determining the existence of a quorum.

Q: What matters are to be voted upon at the Annual Meeting?

A: Three proposals are scheduled for a vote:

Election of eight directors to serve until the next Annual Meeting of Stockholders in 2008;

Adoption of the 2007 Equity Incentive Plan; and

Ratification of the selection of BDO Seidman, LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2008.

As of the date of this Proxy Statement, these three proposals are the only matters which our Board of Directors intends to present at the meeting. Our Board does not know of any other business to be presented at the meeting. If other business is properly brought before the meeting, the persons named on the enclosed proxy card will vote on these other matters in their discretion.

Q: How does the Board recommend that I vote?

A: The Board recommends that you vote FOR the election of each of the nominees for director; FOR the adoption of the 2007 Equity Incentive Plan; and FOR the proposal to ratify the selection of BDO Seidman, LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2008.

Q: How do I vote before the meeting?

A: You may vote your shares by mail by filling in, signing and returning the enclosed proxy card. Most of our stockholders may also vote their shares by telephone or the Internet. The instructions for voting by telephone or the Internet can be found with your proxy card. If you vote by telephone or the Internet, you do not need to return your proxy card. You may either vote "For" all the nominees to the Board of Directors of Forest or you may withhold authority to vote for any nominee(s) you specify. With respect to the adoption of the 2007 Equity Incentive Plan and the ratification of the selection of BDO Seidman, LLP as Forest's independent registered public accounting firm for the fiscal year ending March 31, 2008, you may vote "For" or "Against" or abstain from voting.

Q: May I vote at the meeting?

A: Yes, you may vote your shares at the meeting if you attend in person. **Even if you plan to attend the meeting, we recommend that you also submit your proxy or voting instructions as described below so that your vote will be counted if you later decide not to attend the meeting.**

Q: How many votes do I have?

A: Each share of common stock that you own as of June 21, 2007, entitles you to one vote on each matter voted upon at the Annual Meeting. On June 21, 2007, there were 320,040,471 shares of our Common Stock outstanding.

Q: What should I do if I receive more than one set of proxy materials?

A: You may receive more than one set of these proxy materials, including multiple copies of this Proxy Statement and multiple proxy cards or voting instruction cards. For example, if you hold your shares in more than one brokerage account, you may receive a separate voting instruction card for each brokerage account in which you hold shares. If you are a stockholder of record and your shares are registered in more than one name, you will receive more than one proxy card. Please complete, sign, date and return each proxy card that you receive to ensure that all your shares are voted.

Q: May I change my vote?

A: Yes, you may change your vote or revoke your proxy at any time before the vote at the meeting. You may change your vote prior to the meeting by executing a valid proxy bearing a later date and delivering it to us prior to the meeting at Forest Laboratories, Inc., Attention: Corporate Secretary, 909 Third Avenue, New York, New York 10022. You may withdraw your vote at the meeting and vote in person by giving written notice to our Corporate Secretary. You may also revoke your vote without voting by sending written notice of revocation to our Corporate Secretary at the above address.

Q: How are my shares voted if I submit a proxy but do not specify how I want to vote?

A: If you submit a properly executed proxy card but do not specify how you want to vote, your shares will be voted FOR the election of each of the nominees for director, FOR the adoption of the 2007 Equity Incentive Plan and FOR the ratification of BDO Seidman, LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2008, and in the discretion of the persons named as proxies on all other matters that are properly brought before the meeting.

Q: How do I vote if my broker holds my shares in "street name"?

A: Shares held in "street name" are held in the name of your bank or broker. If your shares are held in a brokerage account in street name, they are not included in the total number of shares listed as owned by you on the enclosed proxy card. Your bank or broker will send you instructions on how to vote those shares.

Q: What vote is required to elect Directors?

A: The eight nominees for election as directors who receive the highest number of "FOR" votes will be elected as directors. This number is a plurality. Abstentions and broker non-votes (defined below) will have no effect on the outcome of the voting to elect directors.

Q: What vote is required to adopt the 2007 Equity Incentive Plan?

A: For approval of this proposal, the proposal must receive the "FOR" vote of a majority of the shares present in person or by proxy and entitled to vote on the matter. Abstentions will have the same effect as a vote against the proposal and broker non-votes will have no effect on the outcome of the vote.

Q: What vote is required to ratify the selection of BDO Seidman, LLP as Forest's independent registered public accounting firm for the fiscal year ending March 31, 2008?

A: For approval of this proposal, the proposal must receive the "FOR" vote of a majority of the shares present in person or by proxy and entitled to vote on the matter. Abstentions will have the same effect as a vote against the proposal and broker non-votes will have no effect on the outcome of the vote.

Q: What is a broker non-vote?

A: When shares are held in "street name", a broker non-vote may occur when a bank or brokerage firm does not vote on a proposal because it does not have discretionary voting power and has not received instructions from the beneficial owner of the shares. A broker non-vote is counted for the purpose of determining whether a quorum is present. Under the current rules of the New York Stock Exchange (NYSE), your broker is permitted to vote your shares on certain routine matters, such as the election of directors and the ratification of BDO Seidman, LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2008, even if you do not instruct the broker how to vote.

Q: Who will count the votes?

A: Votes will be counted by the two independent inspectors of election appointed for the meeting.

Q: Who pays for the solicitation of proxies?

A: We will pay for the entire cost of soliciting proxies. We will also reimburse brokerage firms, banks and other agents for the cost of forwarding proxy materials to beneficial owners. In addition, our directors and employees may solicit proxies in person, by telephone, by Internet, or by other means of communication. Directors and employees will not be paid any additional compensation for soliciting proxies.

Q: How can I find out the results of the voting at the Annual Meeting?

A: Preliminary voting results will be announced at the Annual Meeting. Final voting results will be published in our Quarterly Report on Form 10-Q for the period ending September 30, 2007.

SECURITY OWNERSHIP OF PRINCIPAL STOCKHOLDERS AND MANAGEMENT

The following table sets forth, as of June 21, 2007, the number of common shares owned beneficially by any persons we know to be beneficial owners of more than five percent of our outstanding common shares, each of our directors and each of our executive officers named in the Summary Compensation Table below and all of our directors and named executive officers as a group.

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
5% Stockholders		
Capital Group International, Inc. 11100 Santa Monica Blvd. Los Angeles, CA 90025	52,671,320 (1)	16.46%
Wellington Management Company, LLP 75 State Street Boston, MA 02109	34,360,389 (1)	10.74%
Barclays Global Investors, NA. 45 Fremont Street San Francisco, CA 94105	31,373,301 (1)	9.80%
Capital Guardian Trust Company 11100 Santa Monica Blvd. Los Angeles, CA 90025	28,179,870 (1)	8.81%
Capital Research and Management Company 333 South Hope Street Los Angeles, CA 90071	28,199,800 (1)	8.81%
Clearbridge Advisors, LLC 399 Park Avenue New York, NY 10022	23,740,129 (1)	7.42%
Vanguard Specialized Funds – Vanguard Health Care Fund 100 Vanguard Blvd. Malvern, PA 19355	20,001,500 (1)	6.25%
Named Executive Officers and Directors		
Howard Solomon	6,372,354 (2)	1.99%
Lawrence S. Olanoff, M.D., Ph.D.	7,549 (3)	*
Nesli Basgoz, M.D.	7,500 (4)	*
William J. Candee, III	46,683 (5)	*
George S. Cohan	57,000 (6)	*
Dan L. Goldwasser	56,455 (7)	*

Kenneth E. Goodman	951,470 (8)	*
Lester B. Salans, M.D.	43,000 (9)	*
Francis I. Perier, Jr.	37,500 (10)	*
Ivan Gergel, M.D.	40,500 (11)	*
Elaine Hochberg	481,142 (12)	*
All directors and executive officers as a group	8,101,153 (13)	2.53%

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* Less than 1%

(1) Based upon information set forth in an Information Statement on Schedule 13G filed by the beneficial owner with the SEC.

(2) Includes 5,600,000 shares issuable pursuant to options that are exercisable within 60 days.

(3) Does not include any shares issuable pursuant to options that are exercisable within 60 days.

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(4) Includes 7,500 shares issuable pursuant to options that are exercisable within 60 days.

(5) Includes 42,000 shares issuable pursuant to options that are exercisable within 60 days.

(6) Includes 46,000 shares issuable pursuant to options that are exercisable within 60 days.

(7) Includes 46,000 shares issuable pursuant to options that are exercisable within 60 days. Does not include 21,680 shares owned by Mr. Goldwasser's wife of which Mr. Goldwasser disclaims beneficial ownership.

(8) Does not include any shares issuable pursuant to options that are exercisable within 60 days.

(9) Includes 43,000 shares issuable pursuant to options that are exercisable within 60 days. Does not include 3,200 shares owned by Dr. Salans' wife of which Dr. Salans disclaims beneficial ownership.

(10) Includes 37,500 shares issuable pursuant to options that are exercisable within 60 days.

(11) Includes 40,500 shares issuable pursuant to options that are exercisable within 60 days.

(12) Includes 392,012 shares issuable pursuant to options that are exercisable within 60 days. Ms. Hochberg pledged 45,504 shares as security.

(13) Includes 6,254,512 shares issuable pursuant to options that are exercisable within 60 days.

Section 16(a) Beneficial Ownership Reporting Compliance

Federal securities laws require our executive officers and directors and persons owning more than 10% of our Common Stock to file certain reports on

ownership and changes in ownership with the Securities and Exchange Commission (SEC). Based on a review of our records and other information, we believe that during fiscal 2007, our executive officers, directors and persons holding more than 10% of our common stock timely filed all Section 16(a) reports except for a report on Form 4 covering a sale of shares by George S. Cohan on May 23, 2006 which was inadvertently filed late.

PROPOSAL 1

ELECTION OF DIRECTORS

Our entire Board of Directors is elected each year at the Annual Meeting of Stockholders. The Board is currently comprised of eight members. Each of the nominees listed below is an incumbent director whose nomination to serve for a one-year term was recommended by our Nominating and Governance Committee and approved by the Board. The eight nominees include five independent directors as defined in the NYSE rules and regulations.

Each nominee elected as a director will continue in office until his successor has been elected and qualified or until his or her earlier death, resignation or retirement. Each person nominated has agreed to serve if elected.

The persons named as proxies intend to vote the proxies **FOR** the election of each of the nominees unless you indicate on the proxy card that your vote should be withheld from any or all of the nominees. If for some reason one or more of the nominees is unable to serve, proxies will be voted in favor of the remaining nominees and may be voted for substitute nominees recommended by the Board.

The following persons have been nominated as directors:

Name and Principal Occupation or Position	Age	Has Been a Director Since
Howard Solomon	79	1964
Chairman of the Board and Chief Executive Officer. Mr. Solomon has served as our Chief Executive Officer since 1977.		
Lawrence S. Olanoff, M.D., Ph.D.	55	2006
President and Chief Operating Officer since October 2006. President and Chief Executive Officer at Celsion Corporation from July 2005 to October 2006. For the ten years prior to July 2005, Dr. Olanoff served as Executive Vice President – Chief Science Officer at Forest.		
Nesli Basgoz, M.D.	49	2006
Associate Chief for Clinical Affairs, Division of Infectious Diseases, Massachusetts General Hospital (MGH). Dr. Basgoz previously served as Clinical Director, Infectious Diseases Division of MGH and serves as Associate Professor of Medicine, Harvard Medical School.		

William J. Candee, III	80	1959
Co-Chairman of the Board of Directors and a principal of TXX Services, LLC, a transportation company with operations in New York, New Jersey and Connecticut. For more than 5 years prior to June 2004, Mr. Candee was a member of or of counsel to the law firm of Rivkin Radler, LLP.		
George S. Cohan	83	1977
President, The George Cohan Company, Inc., consultants, since June 1989.		
Dan L. Goldwasser	67	1977
Shareholder, Vedder, Price, Kaufman & Kammholz, P.C., Attorneys at Law, since May 1992.		
Kenneth E. Goodman	59	1998
Until his retirement in September 2006, Mr. Goodman served as President and Chief Operating Officer since December 1998. For eighteen years prior thereto, Mr. Goodman served as Vice President – Finance and Chief Financial Officer and in addition served as Executive Vice President – Operations since February 1998.		
Lester B. Salans, M.D.	71	1998
Clinical Professor and member of the Clinical Attending Staff Internal Medicine, Mount Sinai Medical School and member of the Adjunct Faculty, Rockefeller University. Dr. Salans was Vice President – Academic and Scientific Affairs and Vice President – Preclinical Research at Sandoz Pharmaceutical Corporation.		

CORPORATE GOVERNANCE

We seek to follow best practices in corporate governance in a manner that is in the best interests of our business and our stockholders. We are in compliance with the corporate governance requirements imposed by the Sarbanes-Oxley Act, the SEC and the NYSE and will continue to review our policies and practices to meet ongoing developments in this area.

Code of Business Conduct and Ethics

All of our employees, including our Chief Executive Officer (CEO), Chief Financial Officer (CFO), all other senior financial officers and all other executive officers, are required to comply with our Code of Business Conduct and Ethics. You can access our Code of Business Conduct and Ethics by clicking on the "Corporate Governance" link in the "Investors" section of our website at www.frx.com. The Code of Business Conduct and Ethics is also available in print to any requesting stockholder. We will post any amendments to or waivers of our Code of Business Conduct and Ethics on our website.

Corporate Governance Guidelines

Our Corporate Governance Guidelines reflect the principles by which we operate. From time to time, the Nominating and Governance Committee and the Board reviews and revises our Corporate Governance Guidelines in response to regulatory requirements and evolving best practices. You can access our Corporate Governance Guidelines by clicking on the "Corporate Governance" link in the "Investors" section of our website at www.frx.com. The Corporate Governance Guidelines is also available in print to any requesting stockholder.

Disclosure, Legal Compliance and Risk Management Committee

The Disclosure, Legal Compliance and Risk Management Committee (the Disclosure Committee) is made up of the following members of senior management: Chief Operating Officer (COO), CFO, Senior Vice President – Scientific Affairs, Senior Vice President – Marketing, and Vice President – General Counsel. The primary purpose of the Disclosure Committee is to review and evaluate our disclosure documents, to develop and monitor a program of risk assessment and management and to evaluate legal compliance and compliance with our Code of Business Conduct and Ethics. The Disclosure Committee met four times during the fiscal year ended March 31, 2007. The Disclosure Committee does not have oversight responsibility for financial matters, including financial statements and systems of internal control over financial reporting, which are monitored by the Company’s Audit Committee.

Compliance Committee

We have established a Compliance Committee chaired by our President and COO. Our Compliance Committee is responsible for overseeing our program for compliance with applicable laws and regulations specific to the pharmaceutical industry. The Compliance Committee includes senior management and senior departmental personnel from various corporate divisions (marketing, contract-customer operations, medical and scientific affairs, sample policy compliance, operations, internal audit and legal counsel). Other personnel are invited to participate from time to time as specific issues warrant. The Committee meets approximately every six weeks to review issues related to our Comprehensive Compliance Program, establish and approve compliance policies and provide support, guidance and advice to our Director of Compliance regarding the compliance program.

Certain Relationships and Related Persons Transactions

David Solomon, our CEO’s son, has been employed by Forest since March 26, 2001. Mr. Solomon’s position is Vice President – Forest Pharmaceuticals, Inc., Business Development and Planning. During the 2007 fiscal year, Mr. Solomon’s total compensation was approximately $350,000 and he was awarded 25,000 options under the 2000 Option Plan in connection with his employment by the Company.

BOARD MEETINGS; COMMITTEES

Board of Directors Meetings and Attendance of Directors

The Board held six meetings during the fiscal year ended March 31, 2007. During fiscal 2007, each of the then serving incumbent directors attended 75% or more of the total meetings of the Board and the respective committees on which he or she served. Directors are required to make every reasonable effort to attend the Annual Meeting of Stockholders. All members of the Board who were then in office attended our 2006 Annual Meeting of Stockholders except Dr. Salans.

Director Independence

The Board has affirmatively determined that the following directors have no material relationship with us and are independent within the meaning of Securities Exchange Act Rule 10A-3 and within the NYSE definition of "independence": Nesli Basgoz, M.D., William J. Candee, III, George S. Cohan, Dan L. Goldwasser and Lester B. Salans, M.D. To assist in making the independence determination, the Board has adopted Director Qualification Standards as part of our Corporate Governance Guidelines. The Director Qualification Standards satisfy the NYSE independence requirements. A copy of these standards is attached to this Proxy Statement at Appendix A. Independent directors receive no compensation from us for service on the Board or the Committees other than directors' fees and non-discretionary grants under our stock option plans.

Executive Sessions; Presiding Director

As required by the NYSE listing standards, our non-management directors meet in executive sessions at which only non-management directors are present on a regularly scheduled basis. Our non-management directors choose the presiding director for each meeting by majority vote on a meeting by meeting basis.

Communications with Directors

You may contact the entire Board of Directors, any Committee, the non-management directors as a group or any individual director by calling our Audit Committee Hotline at 1-800-461-0825. An outside vendor collects all reports or complaints and delivers them to the Audit Committee. The Audit Committee will forward all correspondence to the appropriate director or group of directors. You are also welcome to communicate directly with the Board at the Annual Meeting of Stockholders.

Board Committees

The Board has three standing committees: the Audit Committee, the Compensation Committee and the Nominating and Governance Committee. All of the members of the Audit Committee, the Compensation Committee and the Nominating and Governance Committee are independent directors within the meaning of the NYSE Listing Standards and Securities and Exchange Act of 1934 Rule 10A-3. Each of the Committees has the authority to retain independent advisors and consultants, with all fees and expenses to be paid by Forest. The Board-approved charters of each of the Committees are available on our website under the "Investors" link at www.frx.com. The charters are also available in print to any requesting stockholder.

Audit Committee. For the fiscal year ended March 31, 2007, the Audit Committee consisted of William J. Candee, III (the Chairman), Dan L. Goldwasser and Lester B. Salans, M.D. The Board has determined that Dan L. Goldwasser qualifies as an "audit committee financial expert" for purposes of the federal securities laws.

The Audit Committee's primary responsibilities are to: (i) oversee our financial reporting principles and policies and internal control systems, including review of our quarterly and annual financial statements; (ii) review and monitor the performance and independence of our independent registered public accounting firm and the performance of the internal auditing department; (iii) provide an open avenue of communication among the independent registered public accounting firm, financial and senior management, the internal audit department and the Board; and (iv) appoint (subject to stockholder ratification), evaluate, compensate and where appropriate, terminate and replace our independent registered public accounting firm. The Audit Committee held seven meetings during fiscal 2007.

Compensation Committee. The Compensation Committee is composed of Messrs. Candee, Cohan, Goldwasser (the Chairman), and Dr. Salans. Pursuant to the Compensation Committee Charter, the Committee is responsible for (i) discharging the Board's responsibilities relating to compensation of Forest's executive officers and (ii) producing an annual report on executive compensation for inclusion in Forest's Proxy Statement in accordance with applicable rules and regulations. During the fiscal year ended March 31, 2007, the Compensation Committee held two meetings at which the Committee made recommendations concerning annual base salary and bonus for our executive officers for the 2007 calendar year and made recommendations as to the grant of stock options to these executive officers.

Nominating and Governance Committee. The Nominating and Governance Committee is composed of Messrs. Candee (the Chairman), Cohan, Goldwasser and Dr. Salans. The Committee's responsibilities include (i) identifying individuals qualified to become Board members consistent with criteria approved by the Board and recommending that the Board select the director nominees for the next Annual Meeting of Stockholders; (ii) developing and recommending to the Board the Corporate Governance Guidelines; and (iii) overseeing evaluation of the Board and management. The Nominating Committee held one meeting during fiscal 2007.

The Nominating Committee has established a process for identifying and evaluating nominees for director. Although the Nominating Committee will consider nominees recommended by stockholders, the Nominating Committee believes that its process for identifying and evaluating nominees is designed to produce nominees that possess the educational, professional, business and personal attributes that are best suited to further Forest's purposes. Any interested person may recommend a nominee by submitting the nomination, together with appropriate biographical information, to the Nominating and Governance Committee, c/o the Corporate Secretary, Forest Laboratories, Inc., 909 Third Avenue, New York, New York 10022. All recommended candidates will be considered using the criteria set forth in our Corporate Governance Guidelines.

The Nominating Committee will consider, among other factors, the following to evaluate recommended nominees:

The Board's current composition, including expertise, diversity, balance of management and non-management directors;

Independence and other qualifications required or recommended by applicable laws, rules and regulations (including NYSE requirements) and our policies and procedures; and

The general qualifications of potential nominees, including, but not limited to: personal integrity, loyalty to Forest and concern for its success and welfare; experience at strategy and policy setting level; high-level leadership experience in business; breadth of knowledge about issues affecting Forest; an ability to work effectively with others; sufficient time to devote to Forest; and freedom from conflicts of interest.

Named Executive Officers of Forest

Name	Age	Position with Forest
Howard Solomon	79	Chairman of the Board and Chief Executive Officer
Lawrence S. Olanoff, M.D., Ph.D.	55	President and Chief Operating Officer
Ivan Gergel, M.D.	47	Senior Vice President – Scientific Affairs
Elaine Hochberg	50	Senior Vice President – Marketing
Francis I. Perier, Jr.	47	Senior Vice President – Finance and Chief Financial Officer

Set forth below is certain biographical information concerning our executive officers who are not also directors:

Dr. Ivan Gergel was promoted to Senior Vice President – Scientific Affairs on May 19, 2005. From January 2000 until his promotion, Dr. Gergel served as our Vice President – Clinical Development and Medical Affairs and from January 2005 also served as our Chief Medical Officer. Dr. Gergel joined us in June 1998 as Executive Director, Clinical Research. Prior to joining Forest, Dr. Gergel was Group Director – Clinical Research and Medical Affairs at SmithKline Beecham.

Elaine Hochberg is our Senior Vice President – Marketing since December 1999. Ms. Hochberg joined us in June 1997 as Vice President – Marketing of our wholly-owned subsidiary Forest Pharmaceuticals, Inc. In February 1998, she was promoted to Vice President – Marketing. Prior to joining us in 1997, Ms. Hochberg was Assistant Vice President – Marketing at Wyeth-Lederle Laboratories.

Francis I. Perier, Jr. is our Senior Vice President – Finance and Chief Financial Officer since September 2004. From March 2004 until joining us in September 2004, Mr. Perier was Vice President – Finance – Operations Planning – Americas Medicines at Bristol-Myers Squibb. For eight years prior to March 2004, Mr. Perier served in senior financial positions at Bristol-Myers Squibb including four years as Vice President – Finance, Planning, Business Development and Information Technology at its ConvaTec Division. Prior to that, Mr. Perier had been a partner at Deloitte & Touche, LLP.

EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

The Compensation Committee of the Board of Directors (the Compensation Committee) is responsible for setting and administering the policies that govern executive salaries and cash bonus awards and for administering our stock option plans. It will also be responsible for administering our 2007 Equity Incentive Plan, if adopted. The Compensation Committee reviews and approves, or in some cases recommends for the approval of the full Board of Directors, the annual compensation, including equity grants, for our executive officers, including the Chairman of the Board and Chief Executive Officer, the President and Chief Operating Officer, the Senior Vice President – Scientific Affairs, the Senior Vice President – Marketing and the Senior Vice President – Finance and Chief Financial Officer (the Named Executive Officers).

Objectives of Compensation Program

The primary objective of our compensation program, including our executive compensation program, is to structure compensation to allow us to attract, motivate and retain outstanding personnel. Another objective of our compensation program is to directly link compensation to company-wide results as well as to individual performance and to level of responsibility. Our compensation program also aims to align the interests of management and our stockholders and support Forest’s long-term financial performance. Finally, we believe compensation should take into account the value of each employee’s position within Forest and within the marketplace.

What Our Compensation Program is Designed to Reward

As applied to executive officers, our compensation program is designed to reward such officers for their contributions to Forest’s achievements in a highly competitive environment, long-term strategic management and enhancement of stockholder value. In order to measure the contributions of the executive officers, the Compensation Committee reviews our financial information, including changes in revenues and earnings per share during the prior fiscal year and reports relating to achievement of corporate objectives during the prior fiscal year.

In order to evaluate our performance compared to that of our competitors and to evaluate the competitive strength of our compensation levels, the Chairman of the Compensation Committee selects a peer group of mid-size pharmaceutical companies that most closely reflect our size based on annual sales as publicly reported by such companies.(1) Although our operations more closely resemble large pharmaceutical companies and we compete with such companies for executive talent, based on the criteria used for selection, these companies are not included in our peer group. The Compensation

Committee considers such factors in establishing compensation levels. The Compensation Committee does not presently engage a compensation consultant to assist it with discharging its responsibilities relating to executive compensation matters.

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(1) The companies which made up our peer group for fiscal year 2007 were: Amgen Inc., Genentech Inc., Bausch & Lomb Inc., Baxter International Inc., Genzyme Corporation, Allergan Inc., Gilead Sciences Inc., Watson Pharmaceuticals Inc., Mylan Laboratories Inc., Alpharma Inc., and Barr Pharmaceuticals, Inc.

The Chairman of the Compensation Committee prepares and reviews with the Compensation Committee a comparative analysis of our financial performance relative to that of competitors within our peer group during the preceding two fiscal years. The Chairman's report for fiscal 2007 included results of operations for each of the companies within our peer group based on publicly reported information available as of the date of the report for the most recently ended four quarters in 2006 and the comparable period in 2005.

In keeping with our objective to maintain a compensation program that is competitive in our market sector and which continues to enable us to attract and retain top executive talent, the Compensation Committee also reviews compensation levels paid by companies in our peer group to their chief executive officers and chief operating officers. This information is summarized in the report prepared by the Chairman for review with the Compensation Committee and is based on disclosures contained in proxy statements filed for the companies' previous fiscal years.

Elements of Our Compensation Plan, Why We Chose Each Element and How It Relates to Our Objectives

The principal elements comprising executive compensation are base salary, bonus and equity awards. These elements compliment each other and give the Committee flexibility to create compensation packages that reward short-term and long-term performance of the individual and Forest.

Regarding most compensation matters, including executive compensation, management provides recommendations to the Compensation Committee. The Compensation Committee evaluates the performance achievements of the individual and Forest during the year from the perspectives of both long-term growth and current results, and makes recommendations to the Board of Directors.

Base Salary. Base salary is the primary fixed element in our compensation program. Executive salaries are reviewed on an annual basis, as well as at the time of a promotion or other material change in responsibilities. As discussed above, increases in salary are based on an evaluation of the individual's performance and level of pay compared to the salaries paid to persons in similar positions by pharmaceutical companies in our peer group, and have generally been in the middle of the range of the benchmark data. The Compensation Committee also takes into account the methods and percentages used to determine annual base salary increases for all our employees when determining the appropriate percentage increases to be paid to our executives. Merit increases in salary are effective on January 1st of each year. The Compensation Committee makes recommendations to the Board of Directors for approval of salary increases for all of our executive officers**.**

Bonus. Our annual bonus program is "at risk" compensation designed to reward our employees (as well as our executive officers) for achievement of key operational goals that we believe will provide the foundation for creating long-term stockholder value. We do not use a formula to determine bonuses but rather the Compensation Committee reviews performance during the prior year, taking into account revenues, changes in our earnings per share and significant accomplishments. In addition to the foregoing, as is the practice in the context of salary reviews, the Compensation Committee also reviews bonus payments made by companies in our peer group to their chief executive officers and chief operating officers. Finally, the Compensation Committee reviews the procedures and general standards used to determine bonuses with respect to employees at all levels within Forest, and reviews the range of percentages applied to award bonuses at the various levels to assist in determining the appropriate percentages to be applied in determining bonus awards.

Equity Awards. Given the long-term nature of the pharmaceutical business, we believe that incentivizing executives to focus on long-term performance is of particular importance to us. We believe that one of the most effective ways to accomplish this objective is to provide executive officers with equity awards. The Company has historically granted stock options to executive officers to achieve this purpose, as stock options provide value to the executive over time as growth in the market price of our shares reflects the successful achievement of our business objectives. The exercise price of each stock option awarded to our executive officers under our option plan is the average of the high and low prices of a share of our common stock on the NYSE on the date of the option grant. All option grants to executive officers are approved by the Compensation Committee, and except for option grants which are approved by the Committee at special meetings held in connection with a newly hired officer, such option grants are approved at the Compensation Committee's December meeting which is scheduled at the beginning of each fiscal year.

As indicated above, we are proposing for adoption at this meeting, an Equity Incentive Plan which provides for the issuance of restricted stock, as well as other types of incentives, including awards which vest based on satisfaction of performance conditions as determined by the Compensation Committee and set forth in the individual award agreement. We believe this will provide more flexibility to the Compensation Committee in structuring equity compensation to most closely align it with the objectives of our compensation program.

Consistent with the process used to evaluate and determine the annual base salary and bonus elements of compensation, the Chairman of the Compensation Committee includes in his report to the Compensation Committee a comparative analysis of the value of equity awards made by companies in our peer group. As the focus of this element of compensation is primarily the alignment of the interests of our executive officers with the long-term growth of Forest, the Compensation Committee considers its view of the appropriate equity position of our executive officers in light of our market capitalization in determining the size of all awards.

How the Compensation Committee Chose Amounts: Evaluation of Forest's Performance and Basis for 2007 Compensation

The Compensation Committee meets annually in December to determine compensation levels for the next calendar year, and to award bonuses for performance during the prior calendar year. As described above, in December 2006, the Chairman of the Compensation Committee circulated to the members of the Compensation Committee a report highlighting some of the factors he considered relevant to the Committee's determination of executive officer compensation for the calendar year 2007.

The report addressed our financial performance during the preceding four quarters, including the increase in revenues over the comparable period in 2005 and the increase in earnings per share (after expensing payments for product acquisitions completed prior to the date of the report). The report also discussed our successful completion of several product acquisitions, including two late-stage products, while recognizing that these late-stage products had suffered delays in development. The report also noted our success in prosecuting patent litigation concerning Lexapro®. Finally, the report recognized the completion of our program to repurchase thirty million shares of our common stock and the initiation of a new repurchase program.

As discussed above, the report also included comparisons of our sales results for the preceding four quarters as compared to the sales results reported by members in our peer group for a comparable period, as well as providing comparisons of chief executive officer and chief operating officer compensation by members of our peer group. Our sales results fell within the mid-range of the reported sales figures of these companies; however, the report acknowledged that the companies included in the peer group were better comparators for purposes of compensation evaluations than for purposes of evaluating sales growth, as the group was primarily made up of large biotech companies which had explosive growth during the prior two years and generic companies which have more stable revenues and earnings. With respect to compensation comparisons, total cash and number of options awarded were below the average levels paid by members of our peer group to their chief executive officers and below the average with respect to total cash compensation but above average with respect to the equity awards granted with respect to our chief operating officer. The report acknowledged that this was in part justified based on the chief operating officer position at Forest having many personnel reporting directly to him, which is somewhat unique in the pharmaceutical industry.

The Committee specifically reviewed and discussed the findings set forth in the report and outlined above, and additionally took note of the increase in revenues from $2.96 billion in fiscal 2006 to projected revenues of $3.34 billion for fiscal 2007, and an increase in earnings per share from $2.08 at the end of fiscal 2006 to a projected $2.70 at the end of fiscal 2007. The Committee also noted increased sales in connection with Lexapro®, Namenda® and Benicar® and the increase in stockholder value as the share price rose from $40.68 at December 30, 2005 to approximately $49 as of the time of the report.

Named Executive Officer Compensation

As discussed above, historically the Compensation Committee determines compensation for the CEO, the COO and President, and the eleven other executive officers of Forest.

Chief Executive Officer. Following its discussion and analysis of the above factors, and specifically taking note of Mr. Solomon's continued leadership and commitment to advancing our growth through the licensing of new products and entry into strategic alliances for the development of new products, the Compensation Committee approved the following compensation for Mr. Solomon, our CEO: an increase in salary of approximately 5.5% from $1,090,000 to $1,150,000 and a 2006 bonus of $600,000 which reflected an increase of $75,000 over the previous year. The Compensation Committee recognized that the bonus for the previous year had represented a $55,000 decrease from the previous year's bonus. With respect to long term incentive compensation, the Committee granted Mr. Solomon 200,000 stock options. As is the Committee's practice, the size of the option grant reflected the Committee's view of Mr. Solomon's contribution toward achievement of objectives relating to long-term growth strategies during the year and gave consideration to the appropriate size of a grant based on comparable information on grants provided to persons occupying the same position at comparable companies, and taking into account the number of options granted to other executive officers of the Company.

Chief Operating Officer. Effective October 30, 2006, Dr. Olanoff was appointed to the position of President and COO of Forest. The Compensation Committee reviewed the role of the President and COO, taking note of the number of direct reports and the level of responsibility associated with the position. In addition, the Committee reviewed Dr. Olanoff's background and qualifications for the position, acknowledging his significant experience in the pharmaceutical industry, his position immediately prior to rejoining Forest as the chief executive officer of another pharmaceutical company, and his unique understanding of Forest and its operations based on his prior tenure as Executive Vice President – Scientific Affairs and the Chief Science Officer of Forest. Based on its evaluation of the requirements of the position and Dr. Olanoff's qualifications to fulfill such requirements, the Compensation Committee determined to maintain the same salary level previously paid in connection with the position and to provide for a target bonus range which reflected the bonus previously paid to our COO. In addition, the Compensation Committee provided for an equity grant which reflected the Compensation Committee's view of the appropriate level of the equity position of our COO and its objective of aligning the interests of the officer with the long-term growth of Forest.

Based on the above analysis, the Compensation Committee approved an offer letter between Forest and Dr. Olanoff, effective October 30, 2006, pursuant to which Dr. Olanoff was awarded an annual base salary of $750,000, is eligible for an annual bonus targeted at 40% to 50% of his annual base salary, and was granted 250,000 stock options. The offer letter is described under the heading

"Employment Agreement" on Page 17 of this Proxy.

As Dr. Olanoff's annual base salary was established in his offer letter, at its December meeting, the Compensation Committee only determined the 2006 bonus payable to Dr. Olanoff. Based on its review of the Company's performance and Dr. Olanoff's contributions since the commencement of his employment, the Compensation Committee awarded Dr. Olanoff a bonus of $100,000.

Since Mr. Goodman retired from service as Forest's President and COO effective October 30, 2006, the Compensation Committee only determined the bonus payable to Mr. Goodman for his service during calendar year 2006. Based on its evaluation of our performance as described above and Mr. Goodman's contributions to our growth during the year, the Compensation Committee awarded him a bonus of $385,000.

Other Executive Officers. The Compensation Committee also reviewed and approved merit increases to salary, bonuses and equity awards for the other executive officers, including the other Named Executive Officers, based on the criteria and pursuant to the process described above. The compensation approved for each Named Executive Officer is set forth in the Summary Compensation Table on Page 16 of this Proxy.

Post Retirement and Other Benefits

Each of the benefits described below were chosen to support our objective of providing a competitive pay package. All of the following types of benefits have been historically provided by us on the same terms and conditions described below and were not materially changed by the Compensation Committee during the 2007 fiscal year.

Severance Payments. We may terminate each of our Named Executive Officer's employment at any time with or without cause, or by reason of death or disability. Additionally, each executive officer may resign at any time without good cause. In order to attract talented executive personnel and to incentivize such individuals to remain with Forest, we have executed offer letters with several executive officers, including certain of the Named

Executive Officers. These letters provide for a severance guarantee for the three year period commencing as of the executive's start date, or if longer, for a one year severance period following his termination of employment, limited to the payment of the agreed compensation and benefits. The guaranty is triggered if the executive is terminated by us without Cause or resigns for Good Reason (each as defined in the agreement). A more detailed description of the severance arrangements with our Named Executive Officers can be found under the heading "Post-Termination Benefits and Change in Control" on Page 21 of this Proxy.

Deferred Compensation. We maintain a nonqualified Deferred Compensation Plan for the benefit of certain executive officers, including our Named Executive Officers. Under this plan, full time salaried employees who have an annual base salary of at least $150,000 may defer up to 50% of their annual base salary and up to 100% of their annual bonuses. Deferred amounts may be invested among several investment programs at the participant's option. Deferred amounts are not subject to federal or state income tax until a participant withdraws amounts from the plan. We do not match any of these funds. Further information on the deferred compensation payable to our Named Executive Officers can be found under the heading "Nonqualified Deferred Compensation" on Page 21 of this Proxy.

Retiree Medical Benefits. On December 1, 1989 the Board authorized the grant of certain medical insurance benefits to certain senior executive officers and their spouses upon the completion of ten years of service by such officers. The benefit is provided to these executives and their spouses for their lifetimes following termination of the executive's employment with us. The benefit is equivalent to the medical insurance benefits provided to the executives as of the date of their termination or as of December 1, 1989, if more favorable, together with payment of other reasonable health care related costs. The benefit need not be provided to the extent and for any time that the executive obtains comparable insurance from a subsequent employer. We have entered such benefit agreements with each of Messrs. Solomon and Goodman.

Change in Control Agreements. We have entered into employment agreements with several key employees, including each of Mr. Solomon, Dr. Olanoff, Dr. Gergel, Ms. Hochberg and Mr. Perier. Each agreement becomes effective only upon the occurrence of a defined change in control. Each agreement provides that the executive is entitled to salary, bonus and benefits for a three year period following a change in control if the executive's employment terminates during such period without cause or for good reason. Subject to certain exceptions, a change in control is (i) an acquisition of 20% or more of our Common Stock or voting securities by a person or group not acquiring their shares directly from us, (ii) a change in the majority of the current Board or their designated successors not consented to by such current Board or designated successors, and (iii) a liquidation or dissolution of Forest or merger, consolidation or sale of all or substantially all of our assets which involves a greater than 50% change in our stockholders or the replacement of a majority of the current Board or their designated successors.

The purpose of these agreements is to aid in retention and recruitment of executive officers. In addition, we believe that these agreements encourage continued dedication to assignment duties during periods involving a possible change in control of Forest and protect the earned benefits of the officer against adverse changes resulting from a change in control. These agreements are described in further detail under the heading "Change in Control" on Page 22 of this Proxy.

Perquisites. We provide certain executive officers, including the Named Executive Officers with certain perquisites that the Compensation Committee believes are reasonable and consistent with our overall compensation program. We do not believe that the perquisites provided to executive officers form a material part of their compensation. The cost of these perquisites to the Company is set forth in the "Summary Compensation Table" on Page 16 of this Proxy under the heading "All Other Compensation" and are described further in footnote 2 to the table. The Compensation Committee periodically reviews the levels of perquisites and other personal benefits provided to our executive officers.

Certain Tax and Accounting Considerations: Deductibility of Executive Compensation

Section 162(m) of the Internal Revenue Code generally limits the deductibility of compensation (other than qualified performance-based compensation) in excess of $1,000,000 paid in a taxable year to a company's chief executive officer and the four other most highly compensated executive officers. We consider the impact of this deductibility limitation on our compensation program and have taken, and will continue to take, the necessary actions to qualify compensation awards for full deductibility to the extent possible and consistent with our compensation goals. The Compensation Committee will review, modify and implement compensation policies, practices and programs as necessary to ensure our ability to attract and retain talented executives while taking into account the deductibility of compensation payments.

Compensation Committee Report(1)

We have reviewed and discussed with management the Compensation Discussion and Analysis to be included in the Company's 2007 Stockholder Meeting Schedule 14A Proxy Statement, filed pursuant to Section 14(a) of the Securities Exchange Act of 1934 (the Proxy). Based on the reviews and discussions referred to above, we have recommended to the Board of Directors that the Compensation Discussion and Analysis referred to above be included in our Proxy.

Compensation

Committee

Dan L. Goldwasser

(Chairman)

William J. Candee, III
George S. Cohan
Lester B. Salans, M.D.

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(1) Notwithstanding anything to the contrary set forth in any of our previous or future filings under the Securities Act of 1933 or the 1934 Act, the Report on Executive Compensation by the Compensation Committee shall not be incorporated by reference in any such filings.

EXECUTIVE COMPENSATION

The following table sets forth compensation for our CEO, CFO and each of our other three most highly compensated executive officers during fiscal year 2007 (our Named Executive Officers).

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Salary ($)	Bonus ($)	Option Awards ($)(1)	All Other Compensation ($)(2)	Total ($)(3)
Howard Solomon, Chairman and Chief Executive Officer	2007	1,105,000	600,000	3,616,690	80,592	5,402,282
Lawrence S. Olanoff, M.D., Ph.D., President and Chief Operating Officer (4)	2007	317,708	100,000	360,717	37,546	815,971
Kenneth E. Goodman, Former President and Chief Operating Officer (5)	2007	556,500	385,000	942,625	48,584	1,932,709
Ivan Gergel, M.D., Senior Vice President – Scientific Affairs	2007	526,625	250,000	779,535	506,075	2,062,235
Elaine Hochberg, Senior Vice President – Marketing	2007	536,625	250,000	1,803,394	66,788	2,656,807
Francis I. Perier, Jr., Senior Vice President – Finance and Chief Financial Officer	2007	501,250	235,000	684,830	61,267	1,482,347

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(1) Represents the amount of compensation cost recognized by us in fiscal year 2007 related to stock option awards granted in fiscal year 2007 and prior years, as described in Statement of Financial Accounting Standards No. 123R (SFAS 123R). For a discussion of valuation assumptions, see Note 1 to our 2007 Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended March 31, 2007. Please see the "Grants of Plan-Based Awards" table on Page 18 of this Proxy for more information regarding Option Awards granted in fiscal year 2007.

(2) This amount includes group term life insurance and compensation credited to the Named Executive Officers pursuant to our Savings and Profit Sharing Plan. This plan covers our employees and the employees of certain of our subsidiaries. These employees become participants in the plan if they are employed for at least six months prior to the plan year-end. The Board makes contributions to the plan at its discretion, however contributions may not exceed 25 percent of the individual plan participant's gross salary (up to a maximum salary of $220,000), including allocated forfeitures for the plan year. Plan participants vest over a period of one to five years of credited service. This amount also includes perquisites provided to our Named Executive Officers which have an aggregate value exceeding $10,000, including costs associated with company cars (including insurance), company provided lunches, membership dues, the cost of benefits continuation coverage paid for Mr. Goodman following his retirement, car service for Dr. Olanoff and relocation costs paid for Dr. Gergel. The total amount associated with relocation expenses for Dr. Gergel was $451,020 which consisted of $281,046 of actual relocation expenses and $169,974 in connection with related tax payments paid by us. The relocation expenses included $120,548 of costs associated with the purchase of Dr. Gergel’s new residence, $109,438 of costs associated with the sale of his previous residence, and $51,060 of miscellaneous expenses associated with his relocation.

(3) There are no above-market or preferential earnings on deferred compensation. Consequently, the Summary Compensation Table does not include earnings on deferred amounts. In addition, none of the Named Executive Officers are eligible for pension benefits as Forest does not have a defined benefit program.

(4) Dr. Olanoff commenced his employment as our President and Chief Operating Officer effective October 30, 2006.

(5) Mr. Goodman resigned as our President and Chief Operating Officer effective October 30, 2006 and retired from his employment with us effective December 31, 2006.

Narrative Addendum to the Summary Compensation Table

Effective October 30, 2006, Lawrence S. Olanoff, M.D., Ph.D. was appointed as our President and Chief Operating Officer and Kenneth E. Goodman retired from such position. Accordingly, this year we are reporting for six Named Executive Officers.

Employment Agreement

In connection with Dr. Olanoff's appointment, as our President and Chief Operating Officer effective October 30, 2006, we provided an offer letter to Dr. Olanoff. The offer letter was approved by the Compensation Committee and provides for an annual base salary of $750,000. In addition, Dr. Olanoff is eligible to receive an annual bonus based on performance which is targeted at 40%-50% of his annual base salary. Pursuant to the letter Dr. Olanoff was granted options to purchase 250,000 shares of our Common Stock from one of our stockholder-approved employee stock option plans, with an exercise price equal to the average of the high and low price of our Common Stock on October 30, 2006, with options vesting over a period of five years from the date of grant.

In addition, the letter provides for a severance guarantee for the three year period commencing as of the executive's start date or, if longer, for a one year severance period following his termination of employment, limited to the payment of the agreed compensation and benefits. The guarantee is triggered if Dr. Olanoff is terminated without Cause or upon Good Reason (as defined in the Change in Control Agreement referenced below). In the event of termination without Cause or upon Good Reason, Dr. Olanoff will be paid semi-monthly base salary payments and one bonus payment equal to the last paid bonus or 50% of the salary target during the guarantee period. We will also continue health care coverage for Dr. Olanoff and his family during the guarantee period. In the event this guarantee is activated Dr. Olanoff will stay reasonably available to our management during the period of salary continuation.

Pursuant to the agreement, Dr. Olanoff is also eligible to receive other benefits and perquisites to the extent provided by us to our executive officers, including but not limited to, health, retirement, disability, insurance plans and automobile use and insurance.

A separate Change in Control agreement provides for certain payments to be made to Dr. Olanoff if his employment terminates under certain circumstances. These provisions of the Change in Control agreement are described on Page 21 of this Proxy under the heading "Post-Termination and Change in Control".

GRANTS OF PLAN-BASED AWARDS

The following table sets forth certain additional information regarding grants of plan-based awards to our Named Executive Officers for the fiscal year ended March 31, 2007.

Name	Grant Date	All Other Option	Exercise or Base Price	Grant Date Fair Value

		Awards: Number of Securities Underlying Options (#)	of Option Awards ($)	of Option Awards ($)
Howard Solomon	12/08/2006(1)	200,000	51.5350	3,462,880
Lawrence S. Olanoff, M.D., Ph.D.	10/30/2006(2)	250,000	48.4850	4,328,600
Ivan Gergel, M.D.	12/08/2006(2)	75,000	51.5350	1,298,580
Elaine Hochberg	12/08/2006(2)	75,000	51.5350	1,298,580
Francis I. Perier, Jr.	12/08/2006(2)	75,000	51.5350	1,298,580

(1) The award consists of an option that has a term of ten years. The option became fully exercisable on the six month anniversary of the date of the grant.

(2) Each such award consists of an option that has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

Option Plans

The only long-term incentive compensation plans we presently maintain are our 1998 Stock Option Plan, our 2000 Stock Option Plan and our 2004 Stock Option Plan (the Option Plans). Pursuant to the Option Plans, options may be granted to employees, including executive officers, to purchase shares of Common Stock at a price per share fixed by the Board. The exercise price of all options including Incentive Stock Options (ISOs) as defined by Section 422 of the Internal Revenue Code of 1986 (the Code) is the fair market value on the date of the grant. All of our employees, our subsidiaries' employees and our non-employee directors are eligible to receive options under the Plans. The Plans provide that the Board may determine which employees are granted options and the number of shares subject to each option. The purchase price for shares must be paid in cash or by the tender of shares of Common Stock having a fair market value equal to the option exercise price.

We are proposing for adoption at this meeting a 2007 Equity Incentive Plan which, in addition to granting options, would permit us to grant restricted stock awards, stock appreciation rights, and stock equivalent units. If the 2007 Equity Incentive Plan is approved at our annual meeting of stockholders, no further options will be available for grant under the Option Plans. Please see Page 26 of this Proxy for a complete description of the 2007 Equity Incentive Plan and types of awards which will be available under it.

OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

The following table sets forth information regarding each unexercised option held by each of our Named Executive Officers as of March 31, 2007.

Name	Number of Securities Underlying	Number of Securities Underlying	Option Exercise Price	Option Expiration Date

	Unexercised Options (#) Exercisable	Unexercised Options (#) Unexercisable	($)	
Howard Solomon	600,000	- -	12.0860	12/18/2008
	1,200,000	- -	13.1485	12/17/2009
	2,000,000	- -	33.4532	12/15/2010
	600,000	- -	38.1450	12/14/2011
	400,000	- -	48.3400	12/13/2012
	200,000	- -	59.0500	12/12/2013
	200,000	- -	42.5350	12/13/2014
	200,000	- -	40.2900	12/09/2015
	200,000	- -	51.5350	12/08/2016
Lawrence S. Olanoff, M.D., Ph.D.	- -	250,000 (1)	48.4850	10/30/2016
Ivan Gergel, M.D.	18,000	12,000 (2)	48.3400	12/13/2012
	6,750	8,250 (3)	59.0500	12/12/2013
	4,500	10,500 (4)	42.5350	12/13/2014
	- -	63,750 (5)	40.3200	08/08/2015
	- -	75,000 (6)	51.5350	12/08/2016
Elaine Hochberg	137,012	- -	33.4532	12/15/2010
	150,000	- -	38.1450	12/14/2011
	60,000	40,000 (7)	48.3400	12/13/2012
	22,500	27,500 (8)	59.0500	12/12/2013
	15,000	35,000 (9)	42.5350	12/13/2014
	7,500	42,500 (10)	40.2900	12/09/2015
	- -	75,000 (11)	51.5350	12/08/2016
Francis I. Perier, Jr.	30,000	70,000 (12)	44.7400	09/30/2014
	7,500	42,500 (13)	40.2900	12/09/2015
	- -	75,000 (14)	51.5350	12/08/2016

(1) The option was granted on October 30, 2006 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(2) The option was granted on December 13, 2002 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(3) The option was granted on December 12, 2003 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(4) The option was granted on December 13, 2004 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(5) The option was granted on August 8, 2005 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(6) The option was granted on December 8, 2006 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(7) The option was granted on December 13, 2002 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(8) The option was granted on December 12, 2003 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(9) The option was granted on December 13, 2004 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(10) The option was granted on December 9, 2005 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(11) The option was granted on December 8, 2006 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(12) The option was granted on September 30, 2004 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(13) The option was granted on December 9, 2005 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

(14) The option was granted on December 8, 2006 and has a term of ten years. The option vests and is exercisable as to 15% of the shares underlying the option on the first, second, third and fourth annual anniversaries of the grant date and as to the remaining 40% on the fifth annual anniversary of the grant date.

OPTION EXERCISES AND STOCK VESTED

The following table shows the number of shares acquired upon exercise of stock options by each of our Named Executive Officers during the fiscal year ended March 31, 2007.

	Option Awards	
Name	**Number of Shares Acquired on Exercise (#)**	**Value Realized on Exercise ($)(1)**

Howard Solomon	800,000	39,102,960
Lawrence S. Olanoff, M.D., Ph.D.	- -	- -
Kenneth E. Goodman	3,300,000	77,220,846
Ivan Gergel, M.D.	32,250	472,020
Elaine Hochberg	160,384	6,417,480
Francis I. Perier, Jr.	- -	- -

(1) The "value realized on exercise" is the difference between the market price of the underlying security at exercise and the exercise/base price of the option.

NONQUALIFIED DEFERRED COMPENSATION

The following table shows the executive contributions, earnings and account balances for all Named Executive Officers who participate in our Deferred Compensation Plan. The Deferred Compensation Plan allows full time salaried employees who have an annual base salary of at least $150,000, including the executive officers listed below, to defer up to 50% of their annual base salary and up to 100% of their annual bonuses. Deferred amounts may be invested among several investment programs at the participant’s option. Deferred amounts are not subject to federal or state income tax until a participant withdraws amounts from the plan. We do not match any of these funds.

Employees who participate in the Deferred Compensation Plan may invest deferred monies in a range of investment vehicles that generally mirror the choices available to all employees in the 401(k) plan. The investment options in the Deferred Compensation Plan have returns that would be the same as those earned on the same options in the 401(k) plan. The rates of return for deferred funds in the Deferred Compensation Plan ranged from: -0.54% to 22.5%.

Name	Executive Contributions in Last Fiscal Year ($)(1)	Aggregate Earnings in Last Fiscal Year ($)	Aggregate Withdrawals/ Distributions ($)	Aggregate Balance at Last Fiscal Year End ($)
Lawrence S. Olanoff, M.D., Ph.D.	50,000	9,534	25,224(2)	203,475(3)
Elaine Hochberg	25,000	7,487	- -	107,917(4)

(1) The amounts set forth in this column have also been reported as "Salary" in the Summary Compensation Table on Page 16 of this Proxy.

(2) This distribution was made as a result of Dr. Olanoff’s prior resignation from Forest in 2005.

(3) The opening balance in Dr. Olanoff’s account on October 30, 2006 was $169,165. This amount reflects contributions made by Dr. Olanoff during his prior tenure at Forest.

(4) The opening balance in Ms. Hochberg's account on April 1, 2006 was $75,430.

POST-TERMINATION BENEFITS AND CHANGE IN CONTROL

Compensation upon Termination of Employment.

The offer letters pursuant to which certain executive officers joined Forest, including certain of the Named Executive Officers, include a severance guarantee for the three year period commencing as of the executive's start date (Initial Guarantee Period), or if longer, a one year severance period following his termination of employment, limited to severance and certain benefits in the event of a termination of his employment by us without Cause or his termination of employment for Good Reason, each as defined in the agreement (a Qualifying Termination). The agreement also provides for continued health coverage during the severance period. Dr. Olanoff and Mr. Perier are the only Named Executive Officers who are entitled to severance benefits pursuant to such offer letters.

Upon a Qualifying Termination, each such officer is entitled to continue to receive semi-monthly base salary payments for the Initial Guarantee Period or if longer the one year severance period following his or her termination, plus one bonus payment based on the target bonus described in the agreement, plus continued medical coverage for the employee and his family for the same period during which he is eligible to receive salary. The potential amounts payable pursuant to the severance obligations based on a termination date of March 31, 2007 are set forth in the below table.

Name	Salary ($)	Bonus ($)	Continued Health Care Benefits ($)(1)
Lawrence S. Olanoff, M.D., Ph.D.	1,937,500(2)	375,000(3)	39,630
Francis I. Perier, Jr.	520,000	235,000(4)	15,341

(1) Includes amounts payable for health care coverage (medical and dental) for employee and employee's eligible family members.

(2) Dr. Olanoff had 31 months remaining in the Initial Guarantee Period as of March 31, 2007.

(3) This amount is the higher of last annual bonus or 50% of target salary.

(4) This amount is the higher of last annual bonus or 40% of target salary.

Benefits Continuation Agreements

On December 1, 1989 the Board authorized the grant of certain medical insurance benefits to certain senior executive officers and their spouses upon the completion of ten years of service by such officers. The benefit is provided to these executives and their spouses for their lifetimes following termination of the executive's employment with Forest. The benefit is equivalent to the medical insurance benefits provided to the executives as of the date of their termination or as of December 1, 1989, if more favorable, together with payment of reasonable health care related costs. The benefit need not be provided to the extent and for any time that the executive obtains comparable coverage from a subsequent employer. We have entered into such agreements with Messrs. Solomon and Goodman. The amounts payable on behalf of Mr. Solomon, assuming a Qualifying Termination as of March 31, 2007, are reasonably estimated to be equal to $26,476 annually. Mr. Goodman retired from Forest on December 31, 2006, and accordingly, through March 31, 2007, $17,928 has actually been paid by Forest in connection with providing this benefit to Mr. Goodman. Amounts payable on behalf of Mr. Goodman, from and after March 31, 2007 are reasonably estimated to be equal to $21,712 annually.

Change in Control

The Board has determined that it is in both our best interests and the stockholders to assure that we will have the continued dedication of our executive officers, notwithstanding the possibility of a Change in Control. The Board believes it is imperative to diminish the inevitable distraction of the executive officers by virtue of the personal uncertainties and risks created by a pending or threatened Change in Control and to encourage the executive officer's full attention and dedication to us currently and in the event of any threatened or pending Change in Control, and to provide the executive officer with compensation and benefits arrangements upon a Change in Control which ensure that the compensation and benefits expectations of the executive officers be satisfied and which are competitive with those within our peer group. Therefore, in order to accomplish these objectives, the Board has entered into Change in Control agreements with several key employees, including the Named Executive Officers.

Each agreement becomes effective only upon the occurrence of a Change in Control. Each agreement provides that the executive is entitled to salary, bonus and benefits for a three year period following a Change in Control if the executive's employment terminates during such period without Cause or for Good Reason (a Qualifying Termination), each as defined in the agreement. Subject to certain exceptions, a Change in Control is (i) an acquisition of 20% or more of our Common Stock or voting securities by a person or group not acquiring their shares directly from us, (ii) a change in the majority of the current Board or their designated successors not consented to by such current Board or designated successors, (iii) our liquidation or dissolution or (iv) a merger, consolidation or sale of all or substantially all of our assets which involves a greater than 50% change in our stockholders or the replacement of a majority of the current Board or their designated successors.

Upon such Qualifying Termination, the employee shall be granted in a lump sum payment within thirty days after the date of termination that will be equal to the sum of the following: (i) the amount of our accrued compensation obligations to the executive through the termination date, consisting of unpaid base salary, a pro-rated bonus and other accrued compensation through the termination date, plus (ii) an amount equal to three times the executives base salary and annual bonus, plus (iii) the actuarial equivalent of the employee's benefit under any

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retirement plans in which the executive participates, assuming continued participation for the three year period following the termination date. In addition, the executive shall be granted for a three year period continued medical benefits for both the executive and his or her family, provided however coverage is secondary to any coverage the executive obtains from a subsequent employer. Lastly, the employee is provided with outplacement services and any other amounts or benefits required to be paid or provided under any plan or program.

The following table sets forth our reasonable estimate of the potential payments to each of our Named Executive Officers under our Change in Control Agreements if a Change in Control occurred as of March 31, 2007:

Name	Salary($)(1)	Bonus ($)(2)	Continuation of Benefits under Retirement Plans ($)(3)	Continuation of Welfare Benefits ($)(4)
Howard Solomon	3,450,000	1,950,000	155,626	68,550
Lawrence S. Olanoff, M.D., Ph.D.	2,250,000	780,000	121,950	52,994
Ivan Gergel, M.D.	1,639,500	812,500	129,197	48,458
Elaine Hochberg	1,669,500	812,500	129,195	80,023
Francis I. Perier, Jr.	1,560,000	763,750	138,546	48,458

(1) This amount is equal to three times the respective executive officer's salary in effect at March 31, 2007.

(2) This amount is equal to 25% of the 2007 bonus which had accrued prior to March 31, 2007, plus three times the highest bonus awarded during the last three fiscal years. Dr. Olanoff's "highest bonus" was calculated by annualizing his 2007 bonus pursuant to the terms of the change in control agreement since Dr. Olanoff was not employed for the entire fiscal year.

(3) Amounts set forth represent payments in connection with 401(k) savings plan and our profit sharing plans. Mr. Solomon's amount also includes a reasonable estimate of amounts payable in connection with his Benefits Continuation Agreement.

(4) This amount represents payments made in connection with welfare benefits plans including medical, dental and life insurance.

DIRECTOR COMPENSATION

The table below summarizes the compensation paid by us to non-employee directors for the fiscal year ended March 31, 2007.

Name	Fees Earned or Paid in Cash ($)	Option Awards ($)(1)	Total ($)
Kenneth E. Goodman (2)	9,500	- -	9,500
Nesli Basgoz, M.D.	40,036	63,620	103,656
William J. Candee, III	57,500	63,620	121,120
George S. Cohan	48,639	63,620	112,259

Dan L. Goldwasser	52,500	63,620	116,120
Lester B. Salans, M.D.	49,000	63,620	112,620

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(1) Represents the amount of compensation cost recognized by us in fiscal year 2007 related to stock option awards granted in prior years, as described in Statement of Financial Accounting Standards No. 123R (SFAS 123R). For a discussion of valuation assumptions, see Note 1 to our 2007 Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended March 31, 2007.

(2) Mr. Goodman became a non-employee director of Forest on December 31, 2006.

Director Fees

During the fiscal year ended March 31, 2007, we had the following standard compensation arrangement with our non-employee directors: $30,000 for services as director plus a fee of $2,000 for each Board of Directors meeting attended; $1,500 for attendance at a Committee meeting plus a fee of $1,000 for each Committee Chairman

for each Committee meeting attended provided the Committee meeting was not held in conjunction with a Board of Directors meeting. In addition, we have an arrangement to pay $1,000 to any out-of-town non-employee director who was required to come to New York City for a meeting. Mr. Candee received $5,000 in addition to other director fees in consideration of his services as secretary of meetings of the Board of Directors and of Committees of which he is a member.

Automatic Option Grants

In addition, our non-employee directors participate in the 2004 Stock Option Plan (the 2004 Plan). Under the 2004 Plan, an initial grant of options covering 14,000 shares of Common Stock is automatically granted to persons who become non-employee directors of Forest. Each such option grant is at an exercise price equal to the average price of the Common Stock on the NYSE on the date of grant. Twenty-five percent of the 14,000 options become exercisable on the date of the grant and on each anniversary of such date until all such options are exercisable.

The 2004 Plan further provides for the automatic annual grant to each of our non-employee directors of options to purchase 4,000 shares of Common Stock on the date of their annual election or re-election by our stockholders. Each such option grant is at an exercise price equal to the average price of the Common Stock on the NYSE on the date of grant and become exercisable six months after the date of option grant. All options granted under the 2004 Plan to non-employee directors have a term of ten years from the date of grant (but in no event more than three months following the optionee's ceasing to serve as a member of our Board).

At this meeting, stockholders will be asked to adopt the 2007 Equity Incentive Plan which provides for an initial grant of 20,000 options to non-employee directors upon appointment to the Board and for the automatic annual grant of options to purchase 4,000 shares to non-employee directors plus a grant of 1,000 shares of restricted stock. The initial option grant and each annual restricted stock grant will vest in four equal installments over a three year period with the first installment vesting on the six month anniversary of the date of the grant and the remaining three installments vesting on each of the first, second and third annual anniversaries of the date of the grant. Each annual option grant will vest on the six month anniversary at the date of the grant. Upon adoption of the 2007 Equity Incentive Plan, no further options will be granted under the 2004 Plan, the 2000 Plan or the 1998 Plan including options granted pursuant to automatic grant provisions contained in the 2004 Plan. Further description of the 2007 Equity Incentive Plan is set forth on Page 26 of this Proxy.

AUDIT COMMITTEE REPORT(1)

For the fiscal year ended March 31, 2007, the Audit Committee consisted of William J. Candee, III (the Chairman), Dan L. Goldwasser and Lester B. Salans, M.D. The Board has affirmatively determined that Messrs. Candee and Goldwasser and Dr. Salans are independent as defined under the NYSE listing standards. The Committee operates under a written charter adopted by the Board of Directors.

The Committee recommends to the Board, subject to stockholder ratification, the selection of our independent registered public accounting firm. Management is responsible for our internal controls and the financial reporting process. The independent registered public accounting firm is responsible for performing an independent audit of consolidated financial statements in accordance with auditing standards of the Public Company Accounting Oversight Board and for issuing a report thereon. The Committee monitors and oversees these processes.

In this context, the Committee has met and held discussions with management, the internal auditor and BDO Seidman, LLP (BDO), our independent registered public accounting firm. Management represented that the consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America. The Committee reviewed and discussed the audited consolidated financial statements, as well as the unaudited financial statements included in Quarterly Reports on Form 10-Q for each of the first three quarters of the fiscal year, with management and BDO. The Committee discussed with BDO matters required to be discussed by the Statement of Auditing Standards No. 61 (Communication with Audit Committees). BDO also provided the Committee with the written disclosures required by Independence Standard Board Standard No. 1 (Independence Discussions with Audit Committees), and the Committee discussed with BDO its independence.

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board that the audited financial statements be included or incorporated by reference in the Annual Report on Form 10-K for the fiscal year ended March 31, 2007 for filing with the Securities and Exchange Commission. The Board has adopted this recommendation.

The Audit Committee
William J. Candee, III
Dan L. Goldwasser
Lester B. Salans, M.D.

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(1) Notwithstanding anything to the contrary set forth in any of our previous or future filings under the Securities Act of 1933 or the 1934 Act, the Audit Committee Report shall not be incorporated by reference in any such filings.

PROPOSAL 2

ADOPTION OF THE 2007 EQUITY INCENTIVE PLAN

The Board of Directors has adopted, subject to stockholder approval, and recommends the adoption of Forest’s proposed 2007 Equity Incentive Plan (2007 Plan), under which options and stock awards, stock appreciation rights and stock equivalent units may be granted (each, an Award).

Philosophy

The Board of Directors believes that Forest's traditional policy of providing equity incentives to employees and non-employee directors has been a material factor in the our ability to attract, retain and motivate managerial and professional personnel as well as non-employee directors. While we have historically only granted equity incentives in the form of stock options, the Board of Directors recognizes that competition for executive talent and experienced sales representatives continues to be highly competitive and that the market trend is to offer alternative awards, including restricted stock as well as stock based forms of compensation. We believe that adoption of the 2007 Plan is necessary to remain competitive within our industry and to continue to be able to attract and retain employees. In addition, we believe that the adoption of the 2007 Plan which provides alternative forms of equity grants, including grants which can be made subject to performance based vesting, will provide the Compensation Committee with more flexibility in establishing appropriate compensation packages for employees.

In order to provide the most flexibility in determining the types of Awards that will be available for grant, we have determined that all future Awards should be granted under the 2007 Plan. Accordingly if the stockholders approve the adoption of the 2007 Plan, the number of shares available for association with Awards under the 2007 Plan shall be 9,000,000. In addition, we will no longer be authorized to grant the 4,950,000 shares underlying unissued options as of May 31, 2007 under our 2004 Option Plan, our 2000 Option Plan and our 1998 Option Plan (each a Prior Option Plan), and pursuant to the terms of the 2007 Plan, such shares will now be available for the granting of Awards under the 2007 Plan. All outstanding options issued under such Prior Options Plans will not be affected and will continue to be outstanding in accordance with their terms and the terms of the Prior Option Plan pursuant to which they were issued.

The following description of the 2007 Plan is qualified in its entirety by reference to such 2007 Plan, a copy of which is attached to this Proxy Statement as Appendix B and is incorporated by reference herein.

Administration

The 2007 Plan shall be administered by the Compensation Committee which is composed of three independent directors of the Board. Subject to the terms and conditions of the 2007 Plan, the Compensation Committee is authorized to determine to whom among the eligible persons Awards shall be granted, the number of Shares covered by or associated with an Award, the terms of each Award, and whether any Option is intended to be an ISO or a NSO. In addition the Compensation Committee has authority to interpret and specify rules and regulations relating to the 2007 Plan.

Eligibility

All of our employees, non-employee directors, as well as persons who have accepted offers of employment with Forest, are eligible to participate in the 2007 Plan. Currently we have six non-employee directors and 5,126 employees. In making the determination as to employees to whom Awards shall be granted and as to the number of shares of Common Stock (each, a Share) to be covered by or associated with such Awards, the Compensation Committee shall take into account the duties of the respective employees, their present and potential contributions to the success of Forest and such other factors as the Compensation Committee shall deem relevant in connection with accomplishing the purpose of the 2007 Plan.

Shares Available for Issuance

If the 2007 Plan is approved by our stockholders, the number of new shares with respect to which Awards may be granted under the 2007 Plan is 9,000,000 Shares. In addition, as of May 1, 2007, the 4,950,000 Shares that were issuable upon the exercise of Options remaining available for grant under the Prior Option Plans will now be available for issuance under the 2007 Plan and will no longer be so available under the Prior Option Plans. The following Shares may also be used for issuance of Awards under the 2007 Plan: (i) Shares which have been forfeited under a Stock Grant; and (ii) Shares which are allocable to the unexercised portion of an Option issued under the 2007 Plan which has expired or been terminated. As indicated above, upon adoption of the 2007 Plan, we will no longer be authorized to grant options under the Prior Option Plans. Each Share associated with an Award will count as one Share against the total number of shares available for issuance under the 2007 Plan, provided that each Share associated with a Tandem SAR and the associated Option will only count as one share against the total number of shares available for issuance under the 2007 Plan.

Per-Person Award Limitations

Under the 2007 Plan, the number of Shares with respect to which Awards may be granted to any individual may not exceed 600,000 during any calendar year.

Types and Terms of Awards

The Compensation Committee is authorized to grant the following types of awards under the 2007 Plan: Stock Options (Options), including Incentive Stock Options (ISOs) and Non-Incentive Stock Options (NSOs); Stock Appreciation Rights (SARs); Restricted Stock Grants (Stock Grants); and Stock Equivalent Units (Stock Units).

Options. The Compensation Committee is authorized to grant Options, including ISOs which can result in potentially favorable tax treatment to the option holder and NSOs. The exercise price of an Option is determined by the Compensation Committee at the time of grant and may not be less than the fair market value of the Shares on the date the Option is granted. The term of Options granted to employees may not exceed ten years. The exercise price of Options is payable in cash, in Shares or in a combination of the two, as set forth in the individual Award agreement.

Automatic Grant of Options and Restricted Stock Grants to Non-Employee Directors. An initial grant of Options covering 20,000 Shares will automatically be granted to persons who become non-employee directors from and after the approval of the 2007 Plan by the stockholders. The initial option grant will vest over a three year period as to 25% of the shares covered by the grant on the six month anniversary at the date of the grant and as to an additional 25% on each of the first, second and third annual anniversaries at the date of the grant. The 2007 Plan also provides for an automatic annual grant to each of our non-employee directors of Options to purchase 4,000 Shares plus Stock Grants covering 1,000 Shares on the date of their annual re-election by the stockholders. Each Option granted to non-employee directors will have a term of ten years, have an exercise price equal to the fair market value of a Share on the date of grant and will remain exercisable at its stated term following a director's termination of service. Each annual option grant will vest on the six month anniversary at the date of the grant. The Stock Grant will vest in four equal installments over a three year period with the first installment vesting on the six month anniversary of the date of the grant and the remaining three installments vesting on each of the first, second and third annual anniversaries of the date of the grant.

SARs. SARs grant the holder a right to receive an amount payable in cash or stock equal to the appreciation in price of our Shares over a specified time period. SARs may be granted alone or in tandem with Options. SARs will have a maximum term of ten years and an exercise price of not less than the fair market value of a Share on the date of the SAR grant. No dividends or dividend equivalents will be paid under SARs.

Stock Awards. Stock Awards are grants of restricted stock which vest upon the satisfaction of conditions, which may be based on performance factors or continued service for a specified period of time as determined by the Compensation Committee and set forth in an individual Award agreement. The individual Award agreement will also specify appropriate consideration for the Stock Award and a Stock Award may be issued for no cash or a minimal cash consideration as required by applicable law.

Stock Units. Stock Units grant the recipient a right to receive an amount payable in cash or stock equal to the fair market value of our Shares on the settlement date subject to the satisfaction of performance-based conditions or continued service over a specified period of time as determined by the Compensation Committee and as set forth in the individual Award agreement. The term of Stock Units shall not exceed ten years. Stock Units will be structured to comply with Section 409A of the Internal Revenue Code of 1986, as amended (the Code). No dividends or dividend equivalents will be paid under Stock Units.

General Limitations on Post-Termination Exercisability of Employee Awards. Generally, unless otherwise provided in the Award Agreement by the Compensation Committee, in the event of a termination of an employee's employment for any reason other than death, Disability or Retirement (as such terms are defined in the 2007 Plan), Options and SARs, to the extent exercisable, will remain exercisable for three months from such date or until the expiration of the stated term of such Option, whichever period is shorter. Unless otherwise provided by the Compensation

Committee, in the event of termination of an employee's employment for any reason other than death or Disability (in which case time-based conditions are deemed satisfied), Stock Awards are forfeited on the date of termination of an employee's employment to the extent the conditions applicable to such Award have not been satisfied. Subject to compliance with Section 409A of the Code, all Stock Units are to be settled within 75 days of the settlement date set forth in such individual Award agreement. Additionally, all Awards terminate immediately upon termination of employment as a result of gross misconduct or upon a breach of a contractual or other obligation to Forest as established in the individual Award agreement. The Plan provides special rules for vesting and exercisability upon a termination of employment as a result of death, Disability or Retirement as defined in the Plan.

Other Provisions

Change in Control or Dissolution. Under a Change in Control as defined in the 2007 Plan if Awards remain outstanding under the 2007 Plan following the Change in Control, all unvested Awards granted prior to the effective date of the Change in Control will vest in full upon a Qualified Termination (as defined in the 2007 Plan) of the employee's employment within three years of the Change in Control. If Awards do not remain outstanding following the Change in Control and are not replaced with substitute awards of substantially the same value and subject to substantially the same terms, including the vesting schedule and provision for the immediate vesting upon a Qualified Termination within three years of the date of grant of the substitute award, all Awards which have not been replaced with such substitute awards, will immediately vest upon the effective date of the Change in Control. Upon a dissolution of the Company all outstanding Awards will immediately vest. In addition, upon a Change in Control or a dissolution, the Board may cancel any outstanding portion of an Award, except Stock Awards, in consideration for granting the right to receive a cash payment equal to the per share consideration received by the stockholder in connection with such event less the exercise price applicable to such Award. Any other outstanding Awards, other than Stock Awards, not exercised or cancelled upon such an event will be terminated.

Amendments, Adjustments & Termination. The Board may modify, amend or terminate the 2007 Plan, so long as that action does not impair any Awardee's rights under any outstanding Award without the consent of such affected Awardee. The Board may not amend the 2007 Plan without the approval of the stockholders, to the extent such approval is required under applicable NYSE and SEC rules. In the event of a change to our capitalization, the Compensation Committee has authority to make adjustments, if any, as it deems appropriate and pursuant to applicable laws requiring stockholder approval. The 2007 Plan terminates on June 19, 2017 unless earlier terminated by the Board. No Awards will be granted under the Plan after termination however, the term and exercise of Awards granted before termination may extend beyond the termination date.

Future Plan Benefits

Subject to stockholder approval of this Proposal 2, pursuant to the terms of the 2007 Equity Incentive Plan, each non-employee director shall be granted an Automatic Annual Option Grant and an Automatic Restricted Stock Grant. Currently the Company has six non-employee directors, all of whom are eligible to receive an

Automatic Option Grant and an Automatic Restricted Stock Grant on the day of the 2007 Annual Stockholder meeting, assuming approval of this Proposal 2. The table below sets forth the number of options and the value of the Automatic Annual Option Grants to non-employee directors.

NEW PLAN BENEFITS
2007 Equity Incentive Plan

Name and Position	Dollar Value ($)(1)	Number of Units(2)
All Non-Executive Directors as a Group	1,371,900	30,000

(1) Dollar value is determined based on the closing price of a share of common stock listed on the NYSE on June 21, 2007, of $45.73.

(2) Represents the number of Shares of Common Stock underlying the Annual Automatic Option and Stock Grants. All other grants under the 2007 Plan are within the discretion of the Board of Directors and the Compensation Committee and the benefits of such grants are, therefore, not determinable. However, please refer to the "Grants of Plan-Based Awards" table on Page 18 of this Proxy, which provides information on the grants made to the Named Executive Officers under "Executive Compensation" in the last fiscal year ended March 31, 2007.

Federal Income Tax Consequences

The following is a general explanation of the U.S. federal income tax consequences to Awardees under the 2007 Plan who are subject to tax in the United States. The following is intended for the general information of stockholders considering how to vote with respect to the 2007 Plan and not as tax guidance to participants in the 2007 Plan. The following is not intended to be complete and does not take into account federal employment taxes or state, local or foreign tax implications. Tax laws are complex and subject to change and may vary depending on individual circumstances and from locality to locality. In addition, different tax rules may apply in light of variations in transactions that are permitted under the 2007 Plan (such as payment of the exercise price by surrender of previously owned shares).

Incentive Stock Options ("ISOs"). Subject to the limit with respect to the maximum Award that may be granted to any individual in any calendar year, an individual can receive an unlimited number of ISOs during any calendar year. However, the aggregate fair market value (determined at the time of option grant) of shares with respect to which ISOs first become exercisable by an Awardee during any calendar year (under all of Forest's Plans) cannot exceed $100,000. ISO tax treatment is denied by the Code to any options in excess of that dollar limit.

The grant and exercise of an ISO will not result in income for the Awardee or an income tax deduction for Forest. (However, the excess of fair market value of the shares on the exercise date over the exercise price is an item of tax preference, potentially subject to the alternative minimum tax.) The sale or other taxable disposition of shares acquired upon an ISO exercise will not result in ordinary income by the Awardee if the Awardee (i) does not dispose of the shares within two years from the date of option grant or within one year from the date of option exercise, and (ii) the Awardee is an employee of Forest or one of its subsidiaries from the date of option grant and through the date which is three months before the exercise date (the "Holding Requirements"). If the Holding Requirements are met, gain realized on the sale or other taxable disposition of the shares will be subject to tax as long-term capital gain and the Company would not be entitled to any income tax deduction.

If the Awardee disposes of shares acquired upon the ISO exercise without satisfaction of the Holding Requirements, the disposition will be a "disqualifying disposition" and the Awardee will recognize at the time of such disposition (i) ordinary income to the extent of the difference between the exercise price and the lesser of (a) the fair market value of the shares on the date of exercise or (b) the amount realized on such disposition, and (ii) short-term or long-term capital gain to the extent of any excess of the amount realized on the disposition over the fair market value of the shares on the date of exercise. Notwithstanding the foregoing, if the Awardee dies prior to the option exercise but the Awardee was an employee of Forest or one of its subsidiaries from the date of option grant and through the date which is three months before the date of death, then the Holding Requirements will not apply to a sale or other taxable disposition of the shares by the estate of the Awardee or by a person who acquired the option from the Awardee by bequest or inheritance. Forest generally will be entitled to an income tax deduction equal to the amount of ordinary income recognized by the Awardee at the time such income is recognized.

Non-Incentive Stock Options ("NSOs"). Subject to the limit with respect to the maximum Award that may be granted to any individual in any calendar year, there is no limit on the aggregate fair market value of stock covered by NSOs that may be granted to an Awardee or on the aggregate fair market value of NSOs that first become exercisable in any calendar year. Generally, the Awardee will not recognize income and no income tax deduction will be allowed to Forest upon the grant of an NSO. Upon the exercise of an NSO, the Awardee will recognize ordinary income in an amount equal to the excess of the fair market value of the shares at the time of option exercise over the exercise price, and Forest generally will be entitled to an income tax deduction in the same amount. Forest will be required to ensure that any applicable withholding and payroll tax requirements are satisfied. Any difference between the higher of such fair market value or the option exercise price and the price at which the Awardee sells the shares will be taxable as short-term or long-term capital gain or loss.

Stock Appreciation Rights ("SARs"). An Awardee should not be taxed at the time an SAR is granted nor should Forest receive an income tax deduction with respect thereto. Upon exercise of an SAR, the Awardee will recognize ordinary income (treated as compensation) in an amount equal to the cash or the fair market value of the shares received. Forest generally will be entitled to a corresponding income tax deduction at the time that the Awardee recognizes the ordinary income. Forest will be required to ensure that any applicable withholding and payroll tax requirements are satisfied.

Stock Awards. An Awardee receiving a Stock Award subject to time or performance-based vesting conditions will not recognize any income at the time of grant in the absence of a Section 83(b) election (described below). The Awardee generally will recognize ordinary income at the time the vesting conditions expire, in an amount equal to the excess of the fair market value of the shares on that date over the amount (if any) paid by the Awardee for the shares. For purposes of determining gain on a sale of the shares, (i) the Awardee's tax basis in the shares will be equal to the amount included in income upon the expiration of the vesting conditions plus the amount (if any) paid for the shares, and (ii) the Awardee's holding period for the shares will begin when the vesting conditions expire. Any sale or other disposition of the shares will result in long-term or short-term capital gain. With respect to a Stock Award that is subject to time or performance-based vesting conditions, an Awardee may be able to make an election under Section 83(b) of the Code to be taxed at the time of the Stock Award. In that event the Awardee would recognize as ordinary income the excess of the fair market value of the shares as of the date of grant over the amount (if any) paid by the Awardee for the shares and the Awardee’s holding period would begin at the time of the Award. Forest generally will be entitled to a corresponding income tax deduction at the time ordinary income is recognized by the Awardee. Forest will be required to ensure that any applicable withholding and payroll tax requirements are satisfied.

Stock Unit Awards. An Awardee who is awarded Stock Units generally will not recognize any income, and Forest generally will not receive an income tax deduction, until the Awardee receives the shares or cash distributed pursuant to the Award, at which time the fair market value of the shares or the amount of cash received generally will be ordinary income to the Awardee. Forest generally will be entitled to a corresponding income tax deduction at the time that the Awardee recognizes the ordinary income. Forest will be required to ensure that any applicable withholding and payroll tax requirements are satisfied.

Section 162(m) Limit. Under Section 162(m) of the Code, Forest is not entitled to an income tax deduction for compensation paid to any of Forest's five most highly compensated executive officers that is in excess of $1 million per year, unless such compensation is "performance-based compensation." The 2007 Plan has been structured with the intent that Awards granted under the 2007 Plan may meet the requirements for performance-based compensation under Section 162(m) of the Code, including compensation derived from the exercise of Options and SARs (if granted at a fair market value exercise price) and other Awards that are granted, vest or become exercisable upon the achievement of pre-established, objectively determinable targets based on performance criteria. Awards which satisfy these standards generally should be deductible as performance-based compensation and should not be subject to the limitation on deductibility under Section 162(m) of the Code.

Section 409A. Section 409A of the Code does not apply to ISOs, NSOs and SARs that are issued at fair market value (provided there is no deferral of income beyond the exercise or settlement date) or to Stock Awards. Section 409A of the Code may apply to Stock Unit Awards. However, Stock Unit Awards granted under the 2007 Plan are intended to comply with Section 409A of the Code to the extent applicable.

Plan Participation Table

EQUITY COMPENSATION PLAN INFORMATION

The following table sets forth information regarding outstanding options and shares reserved for future issuance under the equity compensation plans as of March 31, 2007. If the 2007 Equity Incentive Plan is adopted the shares listed in column (c) of this table will no longer be available for issuance under these plans.

Plan Category	**Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)**	**Weighted-average exercise price of outstanding options, warrants and rights (b)**	**Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)(2)**
Equity compensation plans approved by security holders(1)	18,224,444	$40.91	4,956,885
Total	18,224,444	$40.91	4,956,885

(1) Based on outstanding options under our 1998, 2000 and 2004 Stock Option Plans.

(2) Represents securities authorized for issuance and not issued as of March 31, 2007 under our 2004 Stock Option Plan, our 2000 Stock Option Plan and our 1998 Stock Option Plan. If the 2007 Equity Incentive Plan is approved by the stockholders, these shares will no longer be available for issuance under our 2004 Stock Option Plan, our 2000 Stock Option Plan and our 1998 Stock Option Plan.

THE BOARD RECOMMENDS THAT THE STOCKHOLDERS VOTE IN FAVOR OF THE 2007 PLAN.

PROPOSAL 3

RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The firm of BDO Seidman, LLP (BDO) has audited our financial statements for each of the three fiscal years ended March 31, 2007. In addition to retaining BDO to audit our consolidated financial statements for the fiscal year 2007, we and our affiliates retained BDO, as well as other accounting and consulting firms, to provide various consulting and other services in the fiscal year 2007, and expect to continue to do so in the future.

The following table presents fees for professional audit services rendered by BDO for the audit of our annual financial statements and review of financial statements included in our Quarterly Reports on Form 10-Q (Audit Fees) for fiscal 2007 and 2006, and fees billed for other services rendered by BDO.

	2007	2006
Audit Fees	$1,217,500	$1,430,745
Audit Related Fees(1)(2)	30,000	48,056
Tax Fees(2)(3)	117,157	137,961
	$1,364,657	$1,616,762
	========	========

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(1) Audit related fees consisted principally of the audit of our benefit plan.

(2) The Audit Committee has considered the non-audit services performed for us by BDO in their evaluation of that firm's independence.

(3) Tax fees consisted primarily of tax return review, state tax matters and tax advisory services.

The Audit Committee’s policy is to pre-approve all audit services and all non-audit services that our independent registered public accounting firm is permitted to perform for us under applicable federal securities regulations. While the general policy of the Audit Committee is to make such determinations at full Audit Committee Meetings, the Audit Committee may delegate its pre-approval authority to one or more members of the Audit Committee, provided that all such decisions are presented to the full Audit Committee at its next regularly scheduled meeting.

The Board desires to continue the services of BDO for the current fiscal year ending March 31, 2008. Accordingly, the Board recommends that you ratify the appointment by the Board of BDO to audit the financial statements of Forest for the current fiscal year. Representatives of BDO are expected to be present at the Annual Meeting, will have the opportunity to make a statement if they desire to do so, and will be available to respond to appropriate questions from the stockholders.

THE BOARD RECOMMENDS THAT STOCKHOLDERS VOTE IN FAVOR OF THE APPOINTMENT OF BDO SEIDMAN, LLP.

MISCELLANEOUS

Annual Report

Forest's 2007 Annual Report is being mailed to stockholders contemporaneously with this Proxy Statement.

Form 10-K

AT YOUR WRITTEN REQUEST, WE WILL PROVIDE WITHOUT CHARGE A COPY OF OUR ANNUAL REPORT ON FORM 10-K AS FILED WITH THE SEC FOR THE FISCAL YEAR ENDED MARCH 31, 2007. PLEASE MAIL YOUR REQUEST TO CORPORATE SECRETARY, FOREST LABORATORIES, INC., 909 THIRD AVENUE, NEW YORK, NEW YORK 10022. YOU MAY ALSO ACCESS OUR 10-K UNDER THE "INVESTORS" LINK ON OUR WEBSITE AT WWW.FRX.COM.

Proposals of Stockholders; Stockholder Business

If you wish to submit a proposal for consideration at our 2008 Annual Meeting of Stockholders, you should submit the proposal in writing to us at the address set forth on page one of this Proxy Statement. Proposals must be received by us on or before March 2, 2008, for inclusion in next year's proxy materials. If you submit a proposal you must, in all other respects, comply with Rule 14a-8 under the Securities Exchange Act of 1934. If you intend to present a proposal at our 2008 Annual Meeting without inclusion of the proposal in our proxy materials, you are required to provide notice of the presenting proposal to us in accordance with our By-Laws no later than June 10, 2008 nor earlier than May 11, 2008.

If a properly submitted stockholder proposal is received after May 11, 2008, we may vote in our discretion as to that proposal all of the shares for which we have received proxies for the 2008 Annual Meeting of Stockholders.

Your vote is important. We urge you to vote by mail, by telephone, or on the Internet without delay.

WILLIAM J.

CANDEE, III,

Secretary

Dated: June 29, 2007

APPENDIX A

DIRECTOR QUALIFICATION STANDARDS

• No Director who is an employee or a former employee of Forest will be considered "independent" until three years after the employment has ended.

• No Director who receives more than $100,000 per year in direct compensation from Forest, other than director and committee fees and pension or other form of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service) until three years after he or she ceases to receive more than $100,000 per year in such compensation will be considered "independent."

• No Director who is, or in the past three years has been, part of an interlocking directorate in which an executive officer of Forest serves on the compensation committee of another company that currently employs the Director will be considered "independent."

• No Director who during the prior three years, was an executive officer or an employee, or whose immediate family member was an executive officer, of a company that made payments to, or received payments from Forest for property or services in an amount which, in any single fiscal year, exceeded the greater of $1 million or 2% of such other company's consolidated gross assets will be considered "independent."

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APPENDIX B

FOREST LABORATORIES, INC.

2007 EQUITY INCENTIVE PLAN

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1. The Plan. This 2007 Equity Incentive Plan (the "Plan") is intended to encourage ownership of stock or stock equivalents of Forest Laboratories, Inc. (the "Company") by employees and non-employee directors of the Company and its subsidiaries and to provide additional incentive for them to promote the success of the business of the Company.

2. Types of Awards. The following types of awards (each, an "Award") may be granted: (a) options intended to qualify as incentive stock options ("ISOs") within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), (b) options not intended to qualify as ISOs ("NSOs" and together with ISOs, "Options"), (c) stock appreciation rights ("SARs"), (d) restricted stock grants ("Stock Grants"), and (e) stock equivalent units ("Stock Units").

3. Stock Subject to the Plan. Subject to the provisions of Section 12 hereof, the total number of shares of Common Stock, par value $.10 per share, of the Company (the "Stock") which may be issued pursuant to Awards issued under the Plan is (a) 9,000,000 plus (b) 4,950,000 which represents the number of authorized shares of Stock that are issuable upon the exercise of options remaining available for grant as at May 31, 2007 under the Company's 2004, 2000 or 1998 Option Plan (each a "Prior Option Plan"). Upon approval of the Plan, no further options will be available for grant under the Prior Option

Plans. Shares of Stock issued under the Plan may be authorized but unissued shares of Stock or Stock held as treasury stock. The following shares of Stock may also be used for issuance of Awards under the Plan: (i) shares of Stock which have been forfeited under a Stock Grant; and (ii) shares of Stock which are allocable to the unexercised portion of an Option issued under the Plan which has expired or been terminated. Subject to the provisions of Section 12, no more than 8,000,000 shares of Stock may be issued upon the exercise of ISOs issued under the Plan. Each share of Stock issuable upon exercise of an Option or subject to a Stock Grant and each share of Stock as to which an SAR or a Stock Unit is associated shall be counted as one share of Stock at the time of grant for purposes of the limit set forth under this Section and the limit set forth under Section 7(b). With respect to the combination of a Tandem SAR and an Option, where the exercise of the Tandem SAR or the Option results in the cancellation of the other, each share of Stock associated with a Tandem SAR and the associated Option will only count as one share of Stock at the time of grant for purposes of the limits set forth in this Section and in Section 7(b).

4. Administration. The Plan shall be administered by a committee (the "Committee") composed of no fewer than three (3) members of the Board of Directors of the Company (the "Board") each of whom meets the definition of "outside director" under the provisions of Section 162(m) of the Code and the definition of "non-employee director" under the provisions of the Securities Exchange Act of 1934, as amended (the "Exchange Act") or rules and regulations promulgated thereunder. Except as otherwise provided herein, the Committee shall have plenary authority in its discretion, among other things, to determine to whom among the eligible persons Awards shall be granted, the number of shares of Stock covered by or associated with an Award, the terms of each Award, and whether any Option is intended to be an ISO or an NSO. The Committee shall have plenary authority, subject to the express provisions of the Plan, to interpret the Plan, to prescribe, amend and rescind any rules and regulations relating to the Plan and to take such other action in connection with the Plan as it deems necessary or advisable. The interpretation, construction and administration by the Committee of any provisions of the Plan or of any Award granted hereunder shall be final and binding on recipients of Awards hereunder.

5. Eligibility. All employees (including, except for purposes of the last sentence of Section 7(a), persons who have accepted offers of employment) and non-employee directors of the Company and its subsidiaries (including subsidiaries which become such after adoption of the Plan) shall be eligible for Awards under the Plan. In making the determination as to employees to whom Awards shall be granted and as to the number of shares of Stock to be covered by or associated with such Awards, the Committee shall take into account the duties of the respective employees, their present and potential contributions to the success of the Company and such other factors as the Committee shall deem relevant in connection with accomplishing the purpose of the Plan. The adoption of the Plan

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shall not be deemed to give any employee any right to an Award, except to the extent and upon such terms and conditions as may be determined by the Committee. Neither the Plan nor any Award granted hereunder is intended to or shall confer upon any Grantee any right with respect to continuation of employment by the Company or any of its subsidiaries.

6. Grant of Options and Stock Grants to Non-Employee Directors.

(a) Grant upon Initial Election. Options to purchase 20,000 shares of Stock, or such number as may hereafter be approved by the Board of Directors, shall automatically be granted under the Plan to each non-employee director who is first appointed or elected to the Board on or after the Effective Date (as such term is defined in Section 13 below) and prior to the expiration of the Plan on the date of such appointment or election of such non-employee director. Subject to Section 8(g), each Option grant pursuant to this Section 6(a) shall be exercisable as to 25% of the number of shares of Stock covered thereby on the six month anniversary of the date of the grant and as to an additional 25% of the number of shares of Stock covered thereby on each of the first, second and third annual anniversaries of the date of the Option grant.

(b) Annual Grant. Options to purchase 4,000 shares of Stock and a Stock Grant covering 1,000 shares of Stock shall automatically be granted under the Plan to each then serving non-employee member of the Board annually on the date of his election or re-election to the Board. Subject to Section 8(g), each Option granted pursuant to this Section 6(b) shall be exercisable as to all shares of Stock covered thereby on the six month anniversary of the date of grant. Subject to Section

10(f), each Stock Grant pursuant to this Section 6(b) shall vest in four equal installments over a three year period with the first installment vesting on the six month anniversary of the date of the grant and the remaining three installments vesting on each of the first, second and third annual anniversary of the date of the grant.

(c) Termination of Non-Employee Director Provisions of Existing Plan. The provisions of this Section 6 shall supersede and replace provisions for the automatic grant of options to the Company's non-employee directors contained in the Company's 2004 Stock Option Plan, and no options shall be granted pursuant to the provisions of such plan on or after the Effective Date.

7. Certain Limits on Awards.

(a) Limit on ISOs. The aggregate Fair Market Value (determined as of the date of the Option grant) of Stock with respect to which ISOs granted to an employee (whether under the Plan or under any other stock option plan of the Company or its subsidiaries) become exercisable for the first time in any calendar year may not exceed $100,000 (or such other amount as the Internal Revenue Service may decide from time to time for purposes of Section 422 of the Code). If any grant of Options is made to a Grantee in excess of the limits provided in the Code, the excess shall automatically be treated as an NSO. Only employees of the Company or any of its subsidiaries shall be eligible to receive the grant of an ISO.

(b) Limit on all Awards. The number of shares of Stock with respect to which an employee may be granted Awards under the Plan during any calendar year shall not exceed 600,000, subject to the provisions of Section 12.

8. Terms and Conditions of Options. The Committee may in its discretion grant Options, which shall be subject to the following terms and conditions and such other terms and conditions as the Committee may prescribe:

(a) Form of Option. Each Option granted pursuant to the Plan shall be evidenced by an agreement (the "Option Agreement") which shall clearly identify the status of the Option granted (i.e., whether an ISO or an NSO) and which shall be in such form as the Committee shall from time to time approve. The Option Agreement shall comply in all respects with the terms and conditions of the Plan and may contain such additional provisions, including, without limitation, restrictions upon the exercise of the Option as the Committee shall deem advisable.

(b) Stated Term. The term of each Option granted to an employee shall be for a maximum of ten years from the date of granting thereof, or a maximum of five years in the case of an ISO granted to a 10% Holder (as such term is defined in Section 17), but may be for a lesser period or be subject to earlier termination as provided by the Committee, the provisions of the Plan or the Option Agreement. The term of each Option granted to a non-employee director shall be ten years from the date of granting thereof.

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(c) Option Exercise Price. Each Option shall state a per share option exercise price, which shall be not less than 100% of the Fair Market Value of a share of Stock on the date of the Option grant, nor less than 110% of such Fair Market Value in the case of an ISO granted to an individual who, at the time the Option is granted, is a 10% Holder. The Fair Market Value of shares of Stock shall be determined by the Committee based upon (i) the average of the high and low prices of the Stock on the New York Stock Exchange on the date of the granting of the Award, or (ii) such other measure of fair market value as may reasonably be determined by the Board (but consistent with the rules under Section 409A of the Code). "Fair Market Value" as used throughout the Plan shall mean the fair market value as determined in accordance with this Section.

(d) Exercise of Options. An Option may be exercised from time to time as to any part or all of the Stock as to which it is then exercisable in accordance with its terms, provided, however, that an Option may not be exercised as to fewer than 100 shares at any time (or for the remaining shares then purchasable under the Option, if fewer than 100 shares). In addition, except as otherwise provided by the Committee, Options granted to employees may not be exercised prior to the expiration of six months from the date of Option grant. The Option exercise price shall be paid in full at the time of the exercise thereof (i) in cash, (ii) by the transfer to the Company of shares of Stock with a Fair Market Value equal to such exercise price, provided that such shares of Stock have been owned by the Grantee for six months and subject to such other restrictions as may be specified by the Company, or (iii) by a combination of cash and the transfer of shares of Stock pursuant to clause (ii) above. The holder of an Option shall not have any rights as a stockholder with respect to the Stock issuable upon exercise of an Option prior to the date of exercise.

(e) Non-Transferability of Options. Except as provided in the following sentence, an Option shall not be transferable other than by will or the laws of descent and distribution and shall be exercisable during the lifetime of the Grantee only by him or his legal representative. NSOs may be transferred by the Grantee by gift to members of the Grantee's immediate family, including trusts for the benefit of such family members and partnerships or limited liability companies in which such family members are the only owners. A transferred NSO shall be subject to all of the same terms and conditions of the Plan and the Option Agreement as if such NSO had not been transferred.

(f) Termination of Employment.

(i) Employment Termination Date. For purposes of the Plan, the date on which a Grantee ceases to be employed by the Company or any of its subsidiaries for any reason following the grant of the Award is referred to as the "Employment Termination Date."

(ii) Disability or Death of Grantee. In the event of an Employment Termination Date as a result of a Grantee's Disability, the Option granted to such Grantee shall continue to vest in accordance with its terms as if such Grantee continued to provide services to the Company and shall remain exercisable for the balance of its stated term, provided that such Grantee provided services to the Company or any of its subsidiaries for a period of at least one year following the grant of the Option and prior to the Employment Termination Date or as otherwise determined by the Committee. In the event of a Grantee's death (A) while providing services to the Company or any of its subsidiaries as an employee or (B) following a termination of employment due to Disability, the Option shall become fully exercisable by the Grantee's estate upon such Grantee's death and shall remain exercisable for a period of twelve (12) months following the Grantee's death (or, if shorter, the remainder of the Option term as set forth in the Option Agreement), provided that such Grantee was employed by the Company or any of its subsidiaries for a period of at least one year following the grant of the Option and prior to the Employment Termination Date or as otherwise determined by the Committee.

(iii) Other Terminations of Employment. Except as set forth in clause (ii) above or as otherwise determined by the Committee, the number of shares of Stock which may be purchased upon the exercise of an Option granted to an employee shall not exceed the number of shares of Stock as to which such Option was exercisable pursuant to the Plan and the Option Agreement as of the Employment Termination Date. If the Grantee's cessation of employment was as a result of the Grantee's Retirement, the Option shall remain exercisable for the balance of its stated term, provided that such Grantee was employed by the Company or any of its subsidiaries for a period of at least one year following the grant of the Option and prior to the Employment Termination Date or as otherwise determined by the Committee. Except as otherwise set forth in this Section 8(f) or in the Option Agreement, an Option granted to an employee shall remain exercisable for three (3) months (or, if shorter, the remainder of the Option term as set forth in the Option Agreement) following the Employment Termination Date. For purposes of the previous sentence only, with respect to NSO grants only, an employee who continues to provide

services to the Company as a non-employee director of the Company or as a consultant to the Company following termination of his employment by the Company or its subsidiary shall be deemed to continue to be an employee of the Company for the period of such provision of services or consultancy.

(iv) Other Limitations. Notwithstanding anything to the contrary in this Section 8(f), if the employment of a Grantee is terminated by the Company or any of its subsidiaries for gross misconduct, including without limitation, violations of applicable Company policies or legal or ethical standards, all rights under the Option shall terminate on the Employment Termination Date. In addition to the foregoing, the Committee may impose such other limitations and restrictions on the exercise of an Option following the Employment Termination Date as it deems appropriate, including a provision for the termination of an Option in the event of the breach by the Grantee of any of his contractual or other obligations to the Company.

(v) Certain Definitions used herein. The term "Retirement" as used herein shall mean the termination of the employment of a Grantee with the Company or its subsidiary (other than as a result of death or Disability or willful misconduct or activity deemed detrimental to the interests of the Company as determined by the Company) on or after (A) the Grantee’s 65th birthday or (B) the Grantee’s 55th birthday if the Grantee has completed ten years of service with the Company or any of its subsidiaries. The term "Disability" as used herein shall have the meaning ascribed to "permanent and total disability" as set forth in Section 22(e)(3) of the Code.

(g) Termination of Service of a Non-Employee Director. The number of shares of Stock which may be purchased upon the exercise of an Option granted to a non-employee director pursuant to Section 6 shall not exceed the number of shares of Stock as to which such Option was exercisable pursuant to the Plan and the Option Agreement as of the date on which the Grantee ceased to serve as a director of the Company. Options exercisable in accordance with the previous sentence shall remain exercisable for the remainder of the Option term as set forth in the Option Agreement.

9. Terms and Conditions of Stock Appreciation Rights. The Committee may in its discretion grant a right to receive the appreciation in the Fair Market Value of shares of Stock (a "Stock Appreciation Right" or "SAR"), which shall be subject to the following terms and conditions and such other terms and conditions as the Committee may prescribe:

(a) Form of SAR. Each SAR granted pursuant to the Plan shall be evidenced by an agreement (the "SAR Agreement") which shall be in such form as the Committee shall from time to time approve. SARs may be granted alone (a "Freestanding SAR") or in combination with an Option (a "Tandem SAR").

(b) Grant and Term of SARs. The term of each Freestanding SAR shall be for a maximum of ten years from the date of granting thereof, but may be for a lesser period or be subject to earlier termination as provided by the Committee or the provisions of the Plan or SAR Agreement. Any Tandem SAR must be granted at the same time as the related Option is granted, and such Tandem SAR or applicable portion thereof shall terminate and no longer be exercisable upon the termination or exercise of the related Option, except that a Tandem SAR granted with respect to less than the full number of shares of Stock covered by the related Option shall not be reduced until the number of shares of Stock then issuable upon exercise of the related Option is equal to or less than the number of shares of Stock covered by the Tandem SAR.

(c) SAR Exercise Price. Each SAR Agreement shall state a per share exercise price, which shall be not less than 100% of the Fair Market Value of a share of Stock on the date of the SAR grant.

(d) Exercise and Value of SARs. An SAR may be exercised from time to time to the extent it is then exercisable in accordance with its terms. No SAR shall be exercised prior to the expiration of six months from the date of the SAR grant. Upon exercise of a Freestanding SAR, the holder will be entitled to receive an amount in cash or shares of Stock, as set forth in the SAR Agreement, equal to the excess of the Fair Market Value of a share of Stock on the date of the exercise less the exercise price, multiplied by the number of shares of Stock covered by such Freestanding SAR. Upon the exercise of a Tandem SAR, the holder may surrender any related Option or portion thereof which is then exercisable and elect to receive in exchange therefore cash or shares of Stock, as set forth in the SAR Agreement, in an amount equal to the excess of the Fair Market Value of such share of Stock on the date of the exercise less the exercise price, multiplied by the number of shares of Stock covered by the related Option or the portion thereof which is so surrendered. Any Option related to a Tandem SAR shall no longer be exercisable to the extent the related Tandem SAR has been exercised. No fractional shares of Stock shall be issued hereunder.

(e) Payment of Stock Appreciation Right. Payment of an SAR shall be in the form of shares of Stock, cash or any combination of shares of Stock and cash. The form of payment upon exercise of such a right shall be determined by the Committee either at the time of grant of the SAR or at the time of exercise of the SAR. All shares of Stock issued upon the exercise of an SAR shall be valued at the Fair Market Value of such Stock at the time of the exercise of the SAR.

(f) Transfer of SARs. All SARs shall be subject to the same restrictions on transfer as are applicable to NSOs pursuant to Section 8(e), provided that Tandem SARs will not be transferable separately from the related Option, and provided further, that Tandem SARs associated with ISOs will not be transferable other than by will or the laws of descent and distribution.

(g) Termination of Employment. The terms and conditions relating to the treatment of Options following Termination of Employment set forth in Section 8(f) shall apply to SARs, and the holders of SARs shall have the same rights and be subject to the same restrictions and limitations as Grantees pursuant to such Section.

(h) No Dividends or Dividend Equivalents. Notwithstanding anything to the contrary herein, no dividends or dividend equivalents will be payable with respect to outstanding SARs.

10. Terms and Conditions of Stock Grants. The Committee may in its discretion grant Stock Grants, which shall be made subject to the following terms and conditions and such other terms and conditions as the Committee may prescribe:

(a) Form of Grant. Each Stock Grant shall be evidenced by an agreement (the "Restricted Stock Agreement") executed by the Company and the Grantee, in such form as the Committee shall approve, which Agreement shall be subject to the terms and conditions set forth in this Section 10 and shall contain such additional terms and conditions not inconsistent with the Plan as the Committee shall prescribe.

(b) Number of Shares Subject to an Award; Consideration. The Restricted Stock Agreement shall specify the number of shares of Stock subject to the Stock Grant. A Stock Grant shall be issued for such consideration as the Committee may determine appropriate and may be issued for no cash consideration or for such minimum cash consideration as may be required by applicable law.

(c) Conditions. Each Stock Grant shall be subject to such conditions as the Committee shall establish (the "Conditions"), which may include, but not be limited to, conditions which are based upon the continued employment of the Grantee over a specified period of time, or upon the attainment by the Company of one or more measures of the Company’s operating performance, such as earnings, revenue, operating or net cash flows, financial return ratios, total stockholder return or such other measures as may be determined by the Committee (the "Performance Conditions"), or upon a combination of such factors. Measures of operating performance may be based upon the performance of the Company or upon the performance of a defined business unit or function for which the Grantee has responsibility or over which the Grantee has influence. The Grantee shall have a vested right to the Stock subject to the Stock Grant to the extent that the Conditions applicable to such Stock Grant have been satisfied. A Grantee shall forfeit all of his right, title and interest in and to any Stock subject to a Stock Grant in the event that (and to the extent that) such Conditions are not satisfied.

(d) Limitations on Transferability. As used herein, the term "Restricted Period" means, with respect to any shares of Stock subject to a Stock Grant, the period beginning on the Award Date and ending on the date on which the Conditions applicable to the Stock Grant have been met. During the Restricted Period, the Grantee will not be permitted to sell, transfer, exchange, pledge, assign or otherwise dispose of any shares of Stock subject to the Stock Grant (except for shares of Stock as to which the Grantee’s rights have vested); provided, however, that the Committee in its discretion may permit the transfer by the Grantee by gift of such shares of Stock to members of the Grantee’s immediate family, including trusts for the benefit of such family members and partnerships or limited liability companies in which such family members are the only owners, it being understood that any shares of Stock so transferred shall remain subject to all of the terms and conditions of the Plan and the applicable

Restricted Stock Agreement as if the shares of Stock had not been transferred. Except as provided in the preceding sentence, any attempt to transfer shares of Stock subject to a Stock Grant prior to the Conditions applicable to such Stock Grant being satisfied shall be ineffective.

(e) Termination of Employment.

(i) Disability or Death of Grantee. In the event of an Employment Termination Date during the Restricted Period as a result of a Grantee's Disability or death, provided the Grantee was employed by the Company or any of its subsidiaries for a period of at least one year following receipt of the Stock Grant and prior to the Employment Termination Date or as otherwise determined by the Committee, all remaining time-based restrictions shall be accelerated and be deemed to have been satisfied as of the Employment Termination Date, and all stock underlying a Stock Grant subject to Performance Conditions which have not been satisfied shall be forfeited and shall be retired by the Company and resume the status of treasury shares as of the Employment Termination Date.

(ii) Other Terminations of Employment. Upon termination of employment during the Restricted Period for any reason other than as set forth in Section 10(e)(i) above, all shares of Stock subject to a Stock Grant as to which the Conditions have not lapsed or been satisfied or waived shall be forfeited by the Grantee and shall be retired by the Company and shall resume the status of treasury shares as of the Employment Termination Date. In the event of the Grantee's cessation of employment for any reason, the Committee may, in its sole discretion when it finds that such an action would be in the best interests of the Company, accelerate or waive in whole or in part any or all time-based or continuous service Conditions or Performance Conditions with respect to all or part of such Grantee's Stock Grant, except as to any Stock Grant that is intended to constitute "performance-based compensation" under Section 162(m) of the Code, and provided the Committee may not exercise such discretion in connection with a termination of employment for gross misconduct, including without limitation, violations of applicable Company policies or legal or ethical standards.

(f) Termination of Service of a Non-Employee Director. With respect to Stock Grants to non-employee directors pursuant to Section 6(b), in the event of a termination of service as director of a Grantee as a result of such Grantee's death, provided the Grantee had served as a director to the Company or any of its subsidiaries for a period of at least one year following receipt of the Stock Grant and prior to the date of such Grantee's termination of service, all remaining time-based restrictions shall be accelerated and be deemed to have been satisfied as of the date of such director's termination of service. Upon termination of service during the Restricted Period in any other case, all shares of Stock subject to a Stock Grant to a non-employee director pursuant to Section 6(b) as to which the Conditions have not lapsed shall be forfeited by the Grantee and shall be retired by the Company and shall resume the status of treasury shares as of the termination date.

(g) Rights as a Stockholder. Except as otherwise provided herein or as the Committee may otherwise determine, a Grantee of a Stock Grant shall have all of the rights of a stockholder of the Company, including the right to vote the shares subject to a Stock Grant and to receive dividends and other distributions thereon, provided that distributions in the form of stock shall be subject to all of the terms and conditions of the Plan and the Restricted Stock Agreement.

11. Terms and Conditions of Stock Equivalent Units. The Committee may in its discretion grant a right to receive the Fair Market Value of shares of Stock upon the Settlement Date (as defined below) subject to satisfaction of applicable Conditions (a "Stock Unit"), which shall be made subject to the following terms and conditions and such other terms and conditions as the Committee may prescribe:

(a) Form of Grant. Each Stock Unit shall be evidenced by an agreement (the "Stock Unit Agreement") executed by the Company and the Grantee, in such form as the Committee shall approve, which Agreement shall be subject to the terms and conditions set forth in this Section 11 and shall contain such additional terms and conditions not inconsistent with the Plan as the Committee shall prescribe.

(b) Number of Shares Subject to an Award; Consideration. The Stock Unit Agreement shall specify the number of shares of Stock associated with the Stock Unit. A Stock Unit shall be issued for such consideration as the Committee may determine appropriate and may be issued for no cash consideration or for such minimum cash consideration as may be required by applicable law.

(c) Term and Conditions. The term of each Stock Unit shall be for a maximum of ten years from the date of granting thereof, but may be for a lesser period or be subject to earlier termination as provided by the Committee, the provisions of the Plan or the Stock Unit Agreement. Each Stock Unit shall be subject to such Conditions as the Committee shall establish, including time-based and Performance Conditions.

(d) Value and Payment. The value of a Stock Unit shall be determined based on the Fair Market Value of a share of Stock on the Settlement Date, multiplied by the number of shares of Stock associated with the Stock Unit. The "Settlement Date" shall be the earlier of the date designated as the "Payment Date" in the Stock Unit Agreement or the Grantee’s Employment Termination Date. Settlement shall be completed by the Company as soon as practicable, but no later than seventy-five days following the Settlement Date, subject however, to the provisions of Section 11(h) below. Stock Units may be settled in shares of Stock or in cash or any combination of the two, or in any other form of consideration as determined by the Committee and set forth in the Stock Unit Agreement.

(e) Limitations on Transferability. The Grantee may not assign the Stock Unit Agreement or transfer, pledge, assign or otherwise dispose of any of his rights under the Stock Unit Agreement, except that the Committee in its discretion may permit the Grantee to transfer the Agreement by gift to members of the Grantee’s immediate family, including trusts for the benefit of such family members and partnerships or limited liability companies in which such family members are owners, it being understood that any Agreement so transferred shall remain subject to all of the terms and conditions of the Plan as if such Agreement had not been transferred. Except as provided in the preceding sentence, any attempt to transfer the Stock Unit Agreement or transfer the Grantee’s rights thereunder shall be ineffective.

(f) Other Limitations. If the employment of a Grantee is terminated by the Company or any of its subsidiaries for gross misconduct, including without limitation, violations of applicable Company policies or legal or ethical standards, as determined by the Company, all rights under the Stock Unit shall terminate on the date of such termination of employment.

(g) No Dividends or Dividend Equivalents. No dividends or dividend equivalents will be paid with respect to Stock Units.

(h) Delay in Payment. Notwithstanding anything to the contrary contained in this Section 11, so long as a payment with respect to a Stock Unit constitutes "non-qualified deferred compensation" for purposes of Section 409A of the Code, no payment will be made with respect to any Stock Unit Award to any person who, on the Settlement Date, is a "specified employee" of the Company or its subsidiaries (within the meaning of Section 409A(a)(2)(B)(i) of the Code and as determined by the Committee) on account of such Grantee’s Employment Termination Date until the date which is six months after the Settlement Date (or, if earlier than the end of such six-month period, the date of such Grantee’s death). In lieu of designating specified employees for purposes of Section 409A of the Code, the Board in its discretion may identify all employees of the Company and its subsidiaries as "specified employees" for purposes of this provision. The provisions of this Section 11(h) will not apply to payments under a Stock Unit Award that occur pursuant to a Change in Control (as defined in Section 12(c) below) or in connection with the dissolution of the Company.

12. Changes in Capitalization, Dissolutions and Change in Control.

(a) Changes in Capitalization**.** In the event of a change in the outstanding stock of the Company (including but not limited to changes in either the number of shares or the value of shares) by reason of any stock split, reverse stock split, dividend or other distribution (whether in the form of shares, other securities or other property, but not including regular cash dividends), extraordinary cash dividend, recapitalization, merger in which the stockholders of the Company immediately prior to the merger continue to own a majority of the voting securities of the successor entity immediately after the merger, consolidation, split-up, spin-off, reorganization, combination, repurchase or exchange of shares or other securities, or other similar corporate transaction or event, if the Committee shall determine in its sole discretion that, in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan, such transaction or event equitably requires an adjustment in the aggregate number and/or class of shares of Stock available under the Plan (including for this purpose the number of shares of Stock available for issuance under the Plan or limit under Section 7(b)) or in the number, class and/or price of shares of Stock subject to outstanding Options and/or Awards), such adjustment shall be made by the Committee and shall be conclusive and binding for all purposes under the Plan. A participant holding an outstanding award has a legal right to an adjustment that preserves without enlarging the value of such award, with the terms and manner of such adjustment to be determined by the Committee.

(b) Dissolution. Notwithstanding any other provision of this Plan or any Award Agreement entered into pursuant to the Plan, to the extent permitted by applicable law, upon a dissolution of the Company: (i) all Options and SARs then outstanding under the Plan shall become fully exercisable as of the effective date of the dissolution; and (ii) all Conditions of all Stock Grants and Stock Units then outstanding shall be deemed satisfied as of the effective date of the dissolution. In addition, the Board may in its discretion cancel all or any portion of a Grantee’s then outstanding Options, SARs and Stock Units, and in consideration of such cancellation, shall cause to be paid to such Grantee pursuant to the plan of dissolution, an amount in cash equal to the difference between the value of the consideration (as determined by the Board) received by the stockholders of the Company for a share of Stock under the plan of dissolution and any applicable exercise price. Options, SARs and Stock Units not exercised or cancelled prior to or upon a dissolution shall be terminated.

(c) Change in Control.

(i) If Awards issued pursuant to the Plan continue to be outstanding following the effective date of a Change in Control, then in the event of a Qualified Termination of a Grantee’s employment with the Company or any of its subsidiaries during the three (3) year period following a Change in Control and prior to the full vesting of an Award granted under the Plan prior to the Change in Control, all outstanding unvested Awards granted to such Grantee prior to the Change in Control shall immediately become fully vested and exercisable to the extent permitted by law, notwithstanding any provisions of the Plan or of the applicable Award Agreement to the contrary.

(ii) If Awards issued pursuant to the Plan do not continue to be outstanding following the effective date of a Change in Control, then to the extent Awards are not substituted or replaced with Qualified Substitute Awards, (A) any Options and SARs not so substituted or replaced shall become fully exercisable as of the date of the Change in Control; and (B) the Conditions of any Stock Grants and Stock Units not so substituted or replaced shall be deemed satisfied as of the effective date of the Change in Control. In addition, the Board (constituted immediately prior to the effectiveness of such Change in Control) may in its discretion cancel all or any portion of a Grantee’s then outstanding Options, SARs and Stock Units, and in consideration of such cancellation, shall cause to be paid to such Grantee upon the effectiveness of such Change in Control, an amount in cash equal to the difference between the value of the consnt>

If we are unable to attract, train and retain employees, we may not be able to grow or successfully operate our business.

The food retail industry is labor intensive, and our success depends in part upon our ability to attract, train and retain a sufficient number of employees who understand and appreciate our culture, are mobile in order to support our growth, and are able to represent our brand effectively and establish credibility with our business partners and consumers. Our ability to meet our labor needs, while controlling wage and labor-related costs, is subject to numerous external factors, including the availability of a sufficient number of qualified persons in the workforce in the markets in which we are located, unemployment levels within those markets, unionization of the available workforce, prevailing wage rates, changing demographics, health and other insurance costs and changes in employment legislation. Various movements have sought to increase retail employee wages, with some effect on minimum wage rates in certain localities, which may also cause wage rates above the minimum to increase in those markets. In the event of increasing wage rates, if we fail to increase our wages competitively, the quality of our workforce could decline, causing our customer service to suffer, while increasing our wages could cause our earnings to decrease. If we are unable to hire and retain employees capable of meeting our business needs and expectations, our business and brand image may be impaired. Any failure to meet our staffing needs or any material increase in turnover rates of our employees may adversely affect our business, results of operations and financial condition.

The loss of key employees could negatively affect our business.

A key component of our success is the experience of our key employees, including our Interim Chief Executive Officer and President, Sean Crane, our Senior Vice President - Real Estate and Development, Randy Young, and our Senior Vice President - Merchandising and Supply Chain, Marc Jones. These employees have extensive experience in our industry and are familiar with our business, systems and processes. The loss of the services of one or more of our key employees could impair our ability to manage our business effectively. We do not maintain key person insurance on any employee.

In addition to these key employees, we have other employees in positions, including those employees responsible for our merchandising, operations, information technology, and real estate departments, which, if vacant, could cause a temporary disruption in our business until such positions are filled.

Union attempts to organize our employees could negatively affect our business.

None of our employees are currently subject to a collective bargaining agreement. As we continue to grow and enter different regions, unions may attempt to organize all or part of our employee base at certain stores or within certain regions. Responding to such organization attempts may distract management and employees and may have a negative financial impact on individual stores, or on our business as a whole.

Various aspects of our business are subject to federal, state and local laws and regulations. Our compliance with these laws and regulations may require additional capital expenditures and could materially adversely affect our ability to conduct our business as planned.

We are subject to federal, state and local laws and regulations relating to matters such as product labeling, weights and measures, zoning, land use, environmental protection, workplace safety, food safety, public health, and alcoholic beverage sales. In particular, the states in which we operate and several local jurisdictions regulate the licensing of supermarkets and the sale of alcoholic beverages. In addition, certain local regulations may limit our ability to sell alcoholic beverages at certain times. We are also subject to laws governing our relationship with employees, including minimum wage requirements, overtime, working conditions, immigration, disabled access and work permit requirements. Compliance with new laws in these areas, or with new or stricter interpretations of existing requirements, could reduce the revenue and profitability of our stores and could otherwise materially adversely affect our business, financial condition or results of operations. Our new store openings could be delayed or prevented or our existing stores could be impacted by difficulties or failures in our ability to obtain or maintain required approvals or licenses. Our stores are subject to unscheduled inspections on a regular basis, which, if violations are found, could result in the assessment of fines, suspension of one or more needed licenses and, in the case of repeated “critical” violations, closure of the store until a re-inspection demonstrates that we have remediated the problem. Additionally, a number of federal, state and local laws impose requirements or restrictions on business owners with respect to access by disabled persons. Our compliance with these laws may result in modifications to our properties, or prevent us from performing certain further renovations. We cannot predict the nature of future laws, regulations, interpretations or applications, or determine what effect either additional government regulations or administrative orders, when and if promulgated, or disparate federal, state and local regulatory schemes would have on our business in the future.

The terms of our revolving credit facility may restrict our current and future operations, which could adversely affect our ability to respond to changes in our business and to manage our operations.

Our revolving credit facility contains, and any additional debt financing we may incur would likely contain, covenants that restrict our operations, including limitations on our ability to grant liens, incur additional debt, pay dividends, redeem our common stock, make certain investments and engage in certain merger, consolidation or asset sale transactions. A failure by us to comply with the covenants or financial ratios contained in our revolving credit facility could result in an event of default, which could adversely affect our ability to respond to changes in our business and manage our operations. Upon the occurrence of an event of default, the lenders could elect to declare all amounts outstanding to be due and payable and exercise other remedies as set forth in our revolving credit facility. If the indebtedness under our revolving credit facility were to be accelerated, our future financial condition could be materially adversely affected.

We will require significant capital to fund our expanding business, which may not be available to us on satisfactory terms or at all.

To support our expanding business and pursue our growth strategy, we will utilize significant amounts of cash generated by our operations to pay our lease obligations, build out new store space, purchase inventory, pay personnel, further invest in our infrastructure and facilities, and pay for the increased costs associated with operating as a public company. We primarily depend on cash flow from operations and borrowings under our revolving credit facility to fund our business and growth plans. If our business does not generate sufficient cash flow from operations to fund these activities, and sufficient funds are not otherwise available to us under our revolving credit facility, we may need additional equity or debt financing. If such financing is not available to us, or is not available to us on satisfactory terms, our ability to operate and expand our business or to respond to competitive pressures would be limited and we could be required to delay, significantly curtail or eliminate planned store openings or operations or other elements of our growth strategy.

We may incur additional indebtedness in the future which could adversely affect our financial health and our ability to react to changes to our business.

We may incur additional indebtedness in the future. Any increase in the amount of our indebtedness could require us to divert funds identified for other purposes for debt service and impair our liquidity position. If we cannot generate sufficient cash flow from operations to service our debt, we may need to refinance our debt, dispose of assets or issue equity to obtain necessary funds. We do not know whether we will be able to take any of such actions on a timely basis, on terms satisfactory to us or at all. Our level of indebtedness has important consequences to you and your investment in our common stock.

For example, our level of indebtedness may:

- require us to use a substantial portion of our cash flow from operations to pay interest and principal on our debt, which would reduce the funds available to us for working capital, capital expenditures and other general corporate purposes;

- limit our ability to pay future dividends;

- limit our ability to obtain additional financing for working capital, capital expenditures, expansion plans and other investments, which may limit our ability to implement our business strategy;

- heighten our vulnerability to downturns in our business, the food retail industry or in the general economy and limit our flexibility in planning for, or reacting to, changes in our business and the food retail industry; or

- prevent us from taking advantage of business opportunities as they arise or successfully carrying out our plans to expand our store base and product offerings.

We cannot assure you that our business will generate sufficient cash flow from operations or that future borrowings will be available to us in amounts sufficient to enable us to make payments on our indebtedness or to fund our operations.

Our stock price has been volatile, and if our stock price declines, you could lose a significant part of your investment.

The market price of our stock may be influenced by many factors and events, some of which are beyond our control, including those described herein and the following:

- the failure of securities analysts to cover or continue to cover our common stock;
- changes in financial estimates by securities analysts;
- the inability to meet market expectations or the financial estimates of analysts who follow our common stock;
- the failure to meet, or delay in meeting, our growth targets;
- strategic actions by us or our competitors;

- announcements by us or our competitors of significant contracts, acquisitions, joint marketing relationships, joint ventures or capital commitments and other publicity regarding us or our competitors;
- variations in our quarterly sales and operating results and those of our competitors;
- general economic and stock market conditions including broad price fluctuations or the sales of substantial amounts of common stock in the public market or the perception that such sales could occur;
- risks related to our business and our industry, including those discussed above;
- changes in conditions or trends in our industry, markets or customers;
- terrorist acts;
- future sales of our common stock or other securities;
- investor perceptions of the investment opportunity associated with our common stock relative to other investment alternatives; and
- guidance, if any, that we provide to the public, any changes in this guidance or our failure to meet this guidance.

As a result of these factors, investors in our common stock may not be able to resell their shares at or above purchase price or may not be able to resell them at all. These broad market and industry factors may materially reduce the market price of our common stock, regardless of our operating performance. In addition, price volatility may be greater if the trading volume of our common stock is low.

Future sales or the perception of future sales of our common stock may depress the price of our common stock.

The market price of our common stock could decline significantly as a result of sales of a large number of shares of our common stock in the market by affiliates of the Company. The sales, or the perception that these sales might occur, could depress the market price. These sales, or the possibility that these sales may occur, also might make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate.

The Berry family, our founding stockholders, has rights to require us to file registration statements registering additional sales of shares of common stock or to include sales of such shares of common stock in registration statements that we may file for ourselves or other stockholders. Subject to compliance with applicable lock-up restrictions, shares of common stock sold under these registration statements can be freely sold in the public market. In the event such registration rights are exercised and a large number of shares of common stock are sold in the public market, such sales could reduce the trading price of our common stock. These sales also could impede our ability to raise future capital. Additionally, we will bear all expenses in connection with any such registrations (other than stock transfer taxes and underwriting discounts or commissions).

Also, in the future, we may issue shares of our common stock in connection with investments or acquisitions. The amount of shares of our common stock issued in connection with an investment or acquisition could constitute a material portion of the then-outstanding shares of our common stock.

A failure of our internal control over financial reporting could materially impact our business or stock price.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. An internal control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all internal control systems, internal control over financial reporting may not prevent or detect misstatements.

Any failure to maintain an effective system of internal control over financial reporting could limit our ability to report our financial results accurately and timely or to detect and prevent fraud, and could expose us to litigation or adversely affect the market price of our common stock. Our management concluded that its internal control over financial reporting was effective as of January 25, 2015. See “Item 9A. Controls and Procedures — Management’s Annual Report on Internal Control Over Financial Reporting.”

Prior to our initial public offering, we were treated as an S-corporation under Subchapter S of the Internal Revenue Code, and claims of taxing authorities related to our prior status as an S-corporation could harm us.

Prior to November 2010, we were treated as an S-corporation. If the unaudited, open tax years in which we were an S-corporation are audited by the Internal Revenue Service, and we are determined not to have qualified for, or to have violated, our S-corporation status, we will be obligated to pay back taxes, interest and penalties, and we do not have the right to reclaim tax distributions we have made to our stockholders during those periods. These amounts could include taxes on all of our taxable income while we were an S-corporation. Any such claims could result in additional costs to us and could have a material adverse effect on our results of operations and financial condition.

We have entered into a tax indemnification agreement with certain stockholders and could become obligated to make payments to them for any additional federal, state or local income taxes assessed against them for fiscal periods prior to the initial public offering.

Prior to November 2010, we were treated as an S-corporation. In the event of an adjustment to our reported taxable income for a period or periods prior to termination of our S-corporation status, our stockholders at that time could be liable for additional income taxes for those prior periods. Pursuant to a tax indemnification agreement into which we entered with certain stockholders, we agreed that upon filing any tax return (amended or otherwise), or in the event of any restatement of our taxable income, in each case for any period during which we were an S-corporation, we will make a payment to each stockholder on a pro rata basis in an amount sufficient so that the stockholder with the highest incremental estimated tax liability (calculated as if the stockholder would be taxable on its allocable share of our taxable income at the highest applicable federal, state and local tax rates and taking into account all amounts we previously distributed in respect of taxes for the relevant period) receives a payment equal to its incremental tax liability. Depending on the respective tax rates of such stockholders, the aggregate amount that we would be required to pay to the stockholders may be greater than the total amount of additional income taxes assessed. We also agreed to indemnify the stockholders for any interest, penalties, losses, costs or expenses (including reasonable attorneys’ fees) arising out of any claim under the agreement.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

Our corporate headquarters are located in Greensboro, North Carolina and, as of January 25, 2015, we operated 169 stores in 27 states. In fiscal 2013 we increased our store base by 22 stores and in fiscal 2014 we increased our store base by 18 stores. The following store list shows the number of stores operated in each state as of January 25, 2015:

State	Total Number of Stores	State	Total Number of Stores
Alabama	6	Mississippi	1
Arkansas	2	New Hampshire	1
California	3	New Jersey	3
Connecticut	2	New York	4
Florida	40	North Carolina	19
Georgia	12	Ohio	6
Illinois	9	Oklahoma	1
Indiana	5	Pennsylvania	4
Iowa	1	South Carolina	7
Kansas	2	Tennessee	8
Kentucky	3	Texas	6
Louisiana	4	Virginia	13
Maryland	4	Wisconsin	2
Massachusetts	1		
		Total	169

We currently lease all of our stores as well as our corporate headquarters. Our typical lease has a primary term of ten to fifteen years, with multiple options to renew that extend the term of our control. We do not believe that any individual store property is material to our financial condition or results of operation. Additionally, in 2013 we started leasing certain buildings under a capital lease agreement, and in other instances we have leased buildings in which we are considered the owner of the building for accounting purposes.

Of the leases for our stores, five expire in fiscal 2015, four expire in fiscal 2016 and the balance expire at varying terms thereafter. We control options to renew and extend the terms of each of the store leases scheduled to expire in fiscal 2015 and 2016.

In addition to new store openings, we occasionally refresh or remodel and relocate existing stores to improve operating performance. Despite the relative youth of our store base, we continuously consider whether any of our stores need to be refreshed, remodeled or relocated. We generally relocate stores to improve site characteristics or if customer demographics in the area have changed. We plan to refresh or remodel ten stores in fiscal 2015.

Item 3. Legal Proceedings.

In the ordinary course of our business, we are subject to lawsuits, investigations and claims, including, but not limited to, intellectual property disputes, contractual disputes, premises claims and employment, environmental, health, product liability and safety matters. Although we cannot predict with certainty the ultimate resolution of any lawsuits, investigations and claims asserted against us, we do not believe any currently pending legal proceeding to which we are a party will have a material adverse effect on our business, prospects, financial condition, cash flows or results of operations, except for the proceedings described in the immediately succeeding paragraph, which could have a material adverse effect on us.

We are party to a lawsuit that was filed against us in U.S. District Court in Connecticut alleging that the manner in which we implemented and applied the fluctuating workweek method for calculating overtime due to our department managers violated the federal Fair Labor Standards Act. The complaint purports to state a collective action on behalf of a class of department managers in stores in states in which we use the fluctuating workweek method of compensation. We believe that the plaintiff's claims are without merit and intend to vigorously defend ourselves in this proceeding. At this time, we cannot predict whether the Court will certify a collective action, how it will rule on the merits of the claim, and/or the scope of the potential loss in the event of an adverse outcome. Should we ultimately be found liable in this matter, our liability could have a material adverse effect on our results of operations for the period or periods in which it is incurred.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Our common stock has been quoted on The NASDAQ Global Select Market under the symbol "TFM" since November 5, 2010, subsequent to our initial public offering. Prior to that date, there was no public market for our common stock. The following table shows the high and low sale prices per share of our common stock as reported on The NASDAQ Global Select Market for each quarter during the fiscal years ended January 25, 2015 and January 26, 2014:

	High	Low
Fiscal year ended January 25, 2015		
January 27, 2014 to April 27, 2014	$36.83	$31.79
April 28, 2014 to July 27, 2014	37.41	28.70
July 28, 2014 to October 26, 2014	36.94	29.47
October 27, 2014 to January 25, 2015	41.76	34.06
Fiscal year ended January 26, 2014		
January 28, 2013 to April 28, 2013	$50.45	$36.51
April 29, 2013 to July 28, 2013	54.85	40.11
July 29, 2013 to October 27, 2013	57.16	46.64
October 28, 2013 to January 26, 2014	52.86	34.72

As of January 25, 2015, we had approximately 9 holders of record of our common stock. We believe that the number of beneficial owners of our common stock is substantially greater than the number of record holders because a large portion of our common stock is held of record in broker ''street names.''

We currently expect to retain future earnings, if any, for use in the operation and expansion of our business and do not anticipate paying any cash dividends on our common stock for the foreseeable future. The declaration and payment of future dividends to holders of our common stock will be at the discretion of our Board of Directors and will depend upon many factors, including our financial condition, earnings, legal requirements, restrictions in our debt agreements and other factors our Board of Directors deems relevant.

Performance Graph

The graph set forth below compares the cumulative total stockholder return on our common stock between November 5, 2010 (the date our stock began trading on the NASDAQ Global Select Market) and January 25, 2015, with the cumulative total return of (i) the NASDAQ Composite Index and (ii) the S&P Food Retail Index, over the same period. This graph assumes the investment of $100 on November 5, 2010 in our common stock at the closing price of $32.11 on such date (rather than the initial public offering price of $22.00 per share), the NASDAQ Composite Index and the S&P Food Retail Index and assumes the reinvestment of dividends, if any.

The comparisons shown in the graph below are based on historical data. We caution that the stock price performance showing in the graph below is not necessarily indicative of, nor is it intended to forecast, the potential future performance of our common stock. Information used in the graph was obtained from the NASDAQ Stock Market website, a source believed to be reliable, but we are not responsible for any errors or omissions in such information. Please also note that, due to the fact the graph begins in November and includes a transition period resulting from a change in fiscal year-end, the horizontal segments of the graph do not represent equal time intervals.

Item 6. Selected Financial Data.

The following tables set forth our selected historical financial and other data, as well as certain pro forma information that reflects the income tax effect of our conversion from an S-corporation to a C-corporation in 2010.

The historical consolidated balance sheets data as of January 25, 2015, and January 26, 2014, and the historical consolidated statements of income data for the years ended January 25, 2015, January 26, 2014 and January 27, 2013, have been derived from our audited consolidated financial statements, which are included in "Item 15. Exhibits and Financial Statement Schedules" of this Form 10-K. The historical consolidated balance sheets data as of January 27, 2013, January 29, 2012, January 30, 2011, and December 31, 2010 and our historical consolidated statements of income for the year ended January 29, 2012, the one month ended January 30, 2011, and the year ended December 31, 2010, have been derived from our audited consolidated financial statements, which are in our previously filed Annual Reports on Form 10-K. Our consolidated financial statements as of and for the years ended January 25, 2015, January 26, 2014, January 27, 2013, and January 29, 2012, the one month ended January 30, 2011, and the year ended December 31, 2010 were audited by Ernst & Young LLP, independent registered public accounting firm.

You should read the selected historical financial and other data in conjunction with the information included in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and "Item 8. Financial Statements and Supplementary Data" included elsewhere in this Form 10-K. Our historical results set forth below are not necessarily indicative of results to be expected for any future period.

	Year Ended (1)					One Month Ended	Year Ended
	January 25, 2015	January 26, 2014	January 27, 2013	January 29, 2012	January 30, 2011 (unaudited) (2)	January 30, 2011	December 31, 2010
	(dollars in thousands, except share and per share amounts)						
Consolidated Statements of Income Data:							
Sales	$1,753,166	$1,511,657	$1,329,131	$1,108,035	$980,403	$78,149	$974,213
Cost of goods sold	1,158,546	996,301	877,433	741,184	659,344	53,302	654,986
Gross profit	594,620	515,356	451,698	366,851	321,059	24,847	319,227
Selling, general and administrative expenses (3) (4)	406,452	349,813	303,495	247,047	245,955	17,623	244,378
Impairments and store closure costs (5)	22,589	27,505	976	437	775	37	792
Depreciation	61,966	54,657	45,741	36,485	33,483	2,729	33,122
Income from operations	103,613	83,381	101,486	82,882	40,846	4,458	40,935
Other expenses (income):							
Interest expense	4,375	3,783	1,498	1,858	2,209	87	2,374
Other income, net	—	—	—	(2)	(171)	(1)	(170)
Income before provision for income taxes	99,238	79,598	99,988	81,026	38,808	4,372	38,731
Recognition of net deferred tax liabilities upon C-corporation conversion (6)	—	—	—	—	19,125	—	19,125
Tax provision (benefit) (6)	36,213	28,791	35,855	29,631	(1,655)	1,712	(3,309)
Net income	$63,025	$50,807	$64,133	$51,395	$21,338	$2,660	$22,915
Net income per share							
Basic and diluted	$1.30	$1.05	$1.33	$1.07	$0.44	$0.06	$0.48
Dividends declared per	$—	$—	$—	$—	$0.83	$—	$1.00

common share							
Shares used in computation of net income per share,							
Basic	48,298,653	48,206,879	48,076,675	48,002,273	47,991,045	47,991,045	47,991,045
Diluted	48,475,735	48,394,338	48,294,299	48,137,519	48,014,349	48,095,459	48,059,882

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	Year Ended (1)					One Month Ended	Year Ended
	January 25, 2015	January 26, 2014	January 27, 2013	January 29, 2012	January 30, 2011 (unaudited) (2)	January 30, 2011	December 31, 2010
	(dollars in thousands, except share and per share amounts)						
Pro Forma Data (unaudited):							
Income before provision for income taxes					$38,808		$38,731
Pro forma provision for income taxes (7)					15,172		15,113
Pro forma net income (7)					$23,636		$23,618
Pro forma net income per share (7)							
Basic and diluted					$0.49		$0.49
Other Operating Data (unaudited):							
Number of stores at end of period	169	151	129	113	100	100	100
Comparable store sales growth (8)	2.9 %	3.2 %	5.7 %	5.4 %	5.0 %	1.4 %	5.0 %
Gross square footage at end of period (in thousands)	3,580	3,200	2,714	2,383	2,129	2,129	2,129
Average comparable store size (gross square feet) (9)	21,085	21,123	21,192	21,256	21,239	21,273	21,205
Comparable store sales per gross square foot during period	$533	$535	$524	$501	$480	$—	$481

(9) Balance Sheet Data (end of period):							
Total assets	$537,452	$469,628	$385,369	$323,340	$258,857	$258,857	$258,002
Total long-term obligations	$33,337	$50,769	$44,088	$64,000	$81,850	$81,850	$82,450
Total stockholders' equity	$328,787	$256,265	$197,859	$126,916	$72,077	$72,077	$69,212

(1) On January 26, 2011, our Board of Directors approved a change in our fiscal year-end from December 31 of each year to the last Sunday in January of each year, commencing with the Company’s 2011 fiscal year, which started January 31, 2011 and ended January 29, 2012.

(2) For comparative purposes, we have presented the selected consolidated statements of income data for the unaudited fifty-two weeks ended January 30, 2011, which was not covered by the auditors’ report.

(3) Selling, general and administrative expenses included $2.1 million of leadership change related costs for the year ended January 25, 2015.

(4) In November 2010, we recorded share-based compensation and related payroll tax expenses of $28.8 million or $17.6 million, net of tax, in connection with our initial public offering. This expense affected the consolidated statements of income for the unaudited fifty-two weeks ended January 30, 2011 and the year ended December 31, 2010.

(5) Impairments and store closure costs for the year ended January 25, 2015 included approximately $13.0 million in store closure and exit costs for stores closed in fiscal 2014 and approximately $9.0 million in impairment charges for certain store related assets. Impairments and store closure costs for the year ended January 26, 2014 included $26.8 million in impairment charges related to certain real estate and store related assets. There was also an additional store closure charge of $0.2 million to adjust the reserve for a previously closed store for the year ended January 26, 2014.

(6) Income tax expense for 2010 included a $19.1 million charge to recognize a net deferred tax liability resulting from the tax reorganization carried out in connection with our initial public offering. In the period after becoming a C-corporation, from November 2010 through January 30, 2011, we recognized a $2.0 million income tax benefit that resulted from our net loss during that period. Additionally, in the period after becoming a C-corporation, from November 2010 through December 2010, we recognized a $3.7 million income tax benefit that resulted from our net loss during that period.

(7) Prior to November 2010, we were treated as an S-corporation for U.S. federal income tax purposes. As a result, our income was not subject to U.S. federal income taxes or state income taxes where S-corporation status is recognized. In general, the corporate income or loss of an S-corporation is allocated to its stockholders for inclusion in their personal federal income tax returns and state income tax returns in those states where S-corporation status is recognized. We terminated our S-corporation status and converted to a C-corporation in November 2010 in connection with our initial public offering, and we are now subject to additional entity-level taxes that will be reflected in our consolidated financial statements. The pro forma provision for income taxes reflects combined federal and state income taxes on a pro forma basis, as if we had been treated as a C-corporation, using blended statutory federal and state income tax rates of 39.1% for the unaudited fifty-two weeks ended January 30, 2011 and 39.0% for the year ended December 31, 2010. These tax rates reflect the sum of the federal statutory rate and a blended state rate based on our calculation of income apportioned to each state for each period.

(8) Our practice is to include sales from a store in comparable store sales beginning on the first day of the sixteenth full month following the store's opening. We believe that comparability is achieved approximately 15 months after opening. When a store that is included in comparable store sales is remodeled or relocated, we continue to consider sales from that store to be comparable store sales. When a store is closed, it is removed from comparable store sales in the period it is closed. There may be variations in the way that our competitors calculate comparable or "same store" sales. As a result, data in this Form 10-K regarding our comparable store sales may not be comparable to similar data made available by our competitors.

(9) Average comparable store size and comparable store sales per gross square foot are calculated using the gross square footage and sales for stores included within our comparable store base for each month during the given period. We have excluded the comparable store sales per gross square foot calculation for the one month period ended January 30, 2011, due to its lack of comparability to the remainder of the financial data.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

This management's discussion and analysis of financial condition and results of operations contains forward-looking statements that involve risks and uncertainties. See "Cautionary Note Regarding Forward-Looking Statements" for a discussion of the uncertainties, risks and assumptions associated with those statements. You should read the following discussion in conjunction with "Item 6. Selected Financial Data" and our audited consolidated financial statements and related notes which are included elsewhere in this Form 10-K. Our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including but not limited to those described under "Cautionary Note Regarding Forward-Looking Statements," "Item 1A. Risk Factors" and included in other portions of this Form 10-K.

Overview

The Fresh Market is a growing specialty retailer focused on creating an extraordinary food shopping experience for our customers. Since opening our first store in 1982, we have offered high-quality food products, with an emphasis on fresh, premium perishables and an uncompromising commitment to customer service. We seek to provide an attractive, convenient shopping environment while offering our customers a compelling price-value combination. As of January 25, 2015, we operated 169 stores in 27 states across the United States.

We believe several key differentiating elements of our business have enabled us to execute our strategy profitably across our expanding store base. We believe that our differentiated shopping experience has helped us to expand our business significantly through favorable word-of-mouth publicity. Within our smaller-box format, we focus on higher-margin food categories and strive to deliver a more personal level of service and a more enjoyable shopping experience. Further, our smaller-box format is adaptable to different retail sites and configurations and has facilitated our successful growth. Additionally, we believe our disciplined, comprehensive approach to planning and merchandising and the support we provide our stores allow us to deliver a consistent shopping experience and financial performance across our store base. Sales increased 16.0%, or $241.5 million, to $1.75 billion for the year ended January 25, 2015, as compared to the year ended January 26, 2014. Comparable store sales increased 2.9% for the year ended January 25, 2015, as compared to the year ended January 26, 2014. Net income increased 24.0%, or $12.2 million, to $63.0 million for the year ended January 25, 2015, from $50.8 million for the year ended January 26, 2014. Diluted earnings per share for the year ended January 25, 2015 increased to $1.30, compared to diluted earnings per share of $1.05 for the year ended January 26, 2014. Net income for the year ended January 25, 2015 included pre-tax charges of $24.5 million ($15.0 million, net of tax), or $0.31 per share on a diluted basis, associated with store closure and exit costs, impairments of certain store related assets and charges related to a change in leadership. Net income for the year ended January 26, 2014 included a pre-tax charge of $27.6 million ($16.8 million, net of tax), or $0.35 per share on a diluted basis, associated with the impairment of certain real estate and store related assets.

In addition to presenting the Company's financial results in conformity with U.S. generally accepted accounting principles (“GAAP”), we have presented our fiscal years ended January 25, 2015 and January 26, 2014 results on an adjusted basis in order to exclude the impact of certain charges associated with store closure and exit costs, impairments of real estate and certain store related assets and charges related to a change in leadership. These measures are not in accordance with, or an alternative to, GAAP and are reconciled to the Company's most recent GAAP financial statements. The Company's management believes that these presentations provide useful information to management, analysts and investors regarding certain additional financial and business trends relating to the Company's results of operations and financial condition. In addition, the Company's management uses these measures to review the Company's financial results and evaluate its business operations. For a reconciliation of adjusted results to GAAP results and a discussion of why we use non-GAAP financial measures, see “Non-GAAP Adjusted Financial Results”, “Year Ended January 25, 2015 Compared to the Year Ended January 26, 2014”, and “Year Ended January 26, 2014 Compared to the Year Ended January 27, 2013.”
Excluding the items noted above, adjusted net income was $78.0 million or $1.61 per share on a diluted basis for the year ended January 25, 2015, as compared to adjusted net income of $67.6 million or $1.40 per share on a diluted basis for the year ended January 26, 2014. The increase in adjusted net income was 15.4% and the increase in adjusted diluted earnings per share was 15.2%.

Strategic Actions

We have taken actions aimed at improving our profitability and future growth prospects. After taking into consideration extensive analysis of expected future cash flows, the long-term strategic importance of individual stores and the anticipated timeline of store openings in California, we closed our remaining stores in California in fiscal 2015. The Company believes it can achieve more consistent financial results and a better return on its investments by continuing to grow in markets within or closer to its existing markets at this time.

Outlook

We intend to continue our focus on profitable growth by expanding our store base, driving comparable store sales and maintaining or gradually increasing our operating margins over time. Consistent with our history of growth, we intend to continue to expand our store base in existing markets and penetrate new markets when suitable opportunities can be found. We view expansion of our store base as a core competency and have nearly quadrupled our store count over the last ten years. We opened 22 new stores in fiscal 2014 and believe there is a significant opportunity to continue to increase our number of stores. In addition, if attractive opportunities arise, we may use lease inducements to acquire leases as a way to expand our store base and penetrate new markets. Our results of operations have been, and may continue to be, affected by the cost, timing and number of new store openings, because new stores generally have different performance profiles and greater variability in sales volumes than our mature stores, and because the overall revenue contributed by new stores may vary from period to period based on the relative timing of new store openings within each period.

Our current and long-term growth strategy is to: (1) expand market presence through opening new stores and enhancing penetration into existing and adjacent markets, (2) enhance financial performance through comparable store sales growth supported by strong customer service, and (3) enhance operating margin through strategic product sourcing and inventory management, while controlling operating costs by focusing on opportunities for continuous improvement and elimination of waste in all our processes. Given the size of the communities that we target, we believe that there is ample opportunity for new store growth in existing and new markets.

We aim to increase our comparable store sales by generating growth in the number and size of customer transactions. Key elements of our strategy include increasing customer awareness, offering new and differentiated products and continuing to provide a distinctive in-store experience. We also intend to increase our operating margins through scale efficiencies, improved systems, continued cost discipline and enhancements to our merchandise offerings. We expect store growth will permit us to benefit from economies of scale in sourcing products and will allow us to leverage our existing infrastructure for scale efficiencies.

We believe that we are well-positioned to capitalize on evolving consumer preferences and other trends currently shaping the food retail industry. These trends include: a growing emphasis on customer convenience and the shopping experience; an expanding number of eating and snacking occasions among consumers beyond the traditional breakfast, lunch, and dinner; an increasing consumer focus on healthy, fresh and quality offerings as well as food attributes such as organic, non-

GMO, and gluten-free offerings; an increasing consumer interest in locally-grown products including regionally and locally sourced food; an improving perception of private-label product quality; and an increase in the average age of the U.S. population driven by an aging Baby Boomer population which, we believe, tends to make a greater number of shopping trips and higher food at home spending per household than younger age groups.

We expect continued sales growth in fiscal 2015. The magnitude of expected growth could vary significantly due to overall economic and competitive conditions, and due to volatility in the supply and costs of commodities such as meat, seafood, cheese and produce. The Company expects that the development and maturation of new stores will also drive future sales growth. We anticipate opening an additional 19 new stores by the end of fiscal 2015, in addition to refreshing or remodeling 10 stores during the same period.

How We Assess the Performance of Our Business

In assessing our performance, we consider a variety of performance and financial measures. The key measures that we assess to evaluate the performance of our business are set forth below:

Sales

Our sales comprise gross sales net of coupons, commissions and discounts.

The food retail industry and our sales are affected by general economic conditions and seasonality, as well as the factors, discussed below, that affect our comparable store sales. Consumer purchases of specialty food products are particularly sensitive to a number of factors that influence the levels of consumer spending, including economic conditions, the level of disposable consumer income, consumer debt, interest rates and consumer confidence. In addition, our business is seasonal and, as a result, our average weekly sales fluctuate during the year and are usually highest in the fourth quarter when customers make holiday purchases.

Comparable Store Sales

Our practice is to include sales from a store in comparable store sales beginning on the first day of the sixteenth full month following the store’s opening. We believe that comparability is achieved approximately fifteen months after opening. When a store that is included in comparable store sales is remodeled or relocated, we continue to consider sales from that store to be comparable store sales. When a store is closed it is removed from comparable store sales in the period it is closed. There may be variations in the way that our competitors calculate comparable or “same store” sales. As a result, data in this Form 10-K regarding our comparable store sales may not be comparable to similar data made available by our competitors.

Various factors may affect comparable store sales, including:

- overall economic trends and conditions, including general price levels in the economy;
- consumer confidence, preferences, and buying trends;
- our competition, including competitor store openings or closings near our stores;

- our competitors expanding their offerings of premium/perishable products;
- the pricing of our products, including the effects of inflation, deflation and our promotional activities which we evaluate and adjust in the ordinary course of our business;
- the number of customer transactions at our stores;
- our ability to provide an assortment of distinctive, high-quality product offerings to generate new and repeat visits to our stores;
- the level of customer service that we provide in our stores;
- our in-store merchandising-related activities;

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- our ability to source products efficiently;
- our opening of new stores in the vicinity of our existing stores;
- the number of stores we open, remodel or relocate in any period; and
- severe or unfavorable weather conditions.

As we continue to pursue our growth strategy, we expect that a significant percentage of our sales growth will continue to come from new stores not included in comparable store sales. Accordingly, comparable store sales is only one measure we use to assess our performance.

Gross Profit

Gross profit is equal to our sales minus our cost of goods sold. Gross margin measures gross profit as a percentage of our sales. Cost of goods sold is directly correlated with sales and includes the direct costs of purchased merchandise, distribution and supply chain costs, buying costs, store supplies and store occupancy costs. Store occupancy costs include rent, common area maintenance, real estate taxes, personal property taxes, insurance, licenses and utilities. Cost of goods sold is exclusive of depreciation, which is reported separately. The components of our cost of goods sold may not be identical to those of our competitors. As a result, data in this Form 10-K regarding our gross profit and gross margin rate may not be comparable to similar data made available by our competitors.

Gross margin rates are driven by economies of scale from our store base, inventory shrinkage as a percentage of sales, productivity through process and merchandising programs, promotional activities, and pricing on select items. Changes in the mix of products sold may also impact our gross margin rate.

Selling, General and Administrative Expenses

Selling, general and administrative expenses include certain retail store and corporate costs, including compensation (both cash and share-based), pre-opening expenses, marketing and advertising, and other corporate administrative costs. Share-based compensation expenses include those arising from grants made under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan. Pre-opening expenses are costs associated with the opening of new stores including costs associated with store labor, travel, recruiting, relocating and training personnel and other miscellaneous costs. Pre-opening costs are expensed as incurred.

Labor and corporate administrative costs generally decrease as a percentage of sales as a result of an increase in our sales. Accordingly, selling, general and administrative expenses as a percentage of sales are usually higher in lower volume quarters and lower in higher-volume quarters. Store-level compensation costs are generally the largest component of our selling, general and administrative expenses. The components of our selling, general and administrative expenses may not be identical to those of our competitors. As a result, data in this Form 10-K regarding our selling, general and administrative expenses may not be comparable to similar data made available by our competitors. We expect that our selling, general and administrative expenses will increase in future periods due to our continuing store growth.

Impairments and Store Closure Costs

We evaluate long-lived assets for impairment whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable. Factors we consider important which could trigger an impairment review include a decision to close a store or negative operating cash flows. The carrying value is not recoverable if it exceeds the undiscounted cash flows resulting from the use of the asset and its eventual disposition. Our estimates of future cash flows attributable to our long-lived assets require significant judgment based on our historical and anticipated results and are subject to many factors. An unexpected decline in sales or other factors could expose us to future impairment charges that could be material.

We record a reserve for future lease obligations associated with stores that have closed. The fair value of the lease liability is estimated using a discount rate to calculate the present value of the remaining noncancelable lease payments at the cease use date for the store, net of an estimate of subtenant income. Our expectations of potential subtenant income are based on various factors including our knowledge of the geographical area in which the closed store property is located, the remaining lease term and existing conditions. We also seek advice from local brokers and agents, commercial market value analysts, and third-party fair value reports to develop our assumptions. Changes in market and economic conditions could cause us to change our assumptions and may require adjustments to the reserves.

Income from Operations
Income from operations consists of gross profit minus selling, general and administrative expenses, impairments and store closure costs and depreciation.
Income Taxes
We must make certain estimates and judgments in determining income tax expense for financial statement purposes. The amount of taxes currently payable or refundable is accrued, and deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Deferred tax assets are also recognized for realizable loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in income tax rates is recognized in our financial statements in the period that includes the enactment date.
Non-GAAP Adjusted Financial Results

In addition to presenting our financial results in conformity with GAAP in this Form 10-K, we are also presenting results on an “adjusted” basis in order to exclude the impact of charges associated with store closure and exit costs, impairments of certain real estate and store related assets and charges related to a change in leadership for the years ended January 25, 2015 and January 26, 2014. Additionally, these charges reflect an estimated provision for income taxes for fiscal years 2014 and 2013. Except where the context otherwise requires, the use of the term “adjusted” or “as adjusted” with reference to the financial results discussed in this management’s discussion and analysis refers to the adjusted results described in this paragraph. These adjusted financial results are non-GAAP financial measures. These measures are not in accordance with, or an alternative to, GAAP and are reconciled to the Company's most recent GAAP financial statements. The Company's management believes that these presentations provide useful information to management, analysts and investors regarding certain additional financial and business trends relating to the Company's results of operations and financial condition. In addition, the Company's management uses these measures to review the Company's financial results and evaluate its business operations. We believe that the presentation of adjusted financial results facilitates an understanding of our operations without the impact associated with the charges referenced above. Non-GAAP financial measures should not be considered in isolation from, or as a substitute for, financial information prepared in accordance with GAAP.

Results of Operations

The following tables summarize key components of our results of operations for the periods indicated, both in dollars and as a percentage of sales.

	Year Ended January 25, 2015		January 26, 2014		January 27, 2013	
	(dollars in thousands, except share and per share amounts)					
Consolidated Statements of Income Data:						
Sales	$1,753,166	100.0%	$1,511,657	100.0%	$1,329,131	100.0%
Cost of goods sold	1,158,546	66.1 %	996,301	65.9 %	877,433	66.0 %
Gross profit	594,620	33.9 %	515,356	34.1 %	451,698	34.0 %
Selling, general and administrative expenses (1)	406,452	23.2 %	349,813	23.1 %	303,495	22.8 %
Impairments and store closure costs (2)	22,589	1.3 %	27,505	1.8 %	976	0.1 %
Depreciation	61,966	3.5 %	54,657	3.6 %	45,741	3.4 %
Income from operations	103,613	5.9 %	83,381	5.5 %	101,486	7.6 %
Interest expense	4,375	0.2 %	3,783	0.3 %	1,498	0.1 %
Income before provision for income taxes	99,238	5.7 %	79,598	5.3 %	99,988	7.5 %
Tax provision	36,213	2.1 %	28,791	1.9 %	35,855	2.7 %
Net income	$63,025	3.6 %	$50,807	3.4 %	$64,133	4.8 %
Net income per share:						
Basic and diluted	$1.30		$1.05		$1.33	
Shares used in computation of net income per share,						
Basic	48,298,653		48,206,879		48,076,675	
Diluted	48,475,735		48,394,338		48,294,299	

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Other Operating Data (unaudited):			
Number of stores at end of period	169	151	129
Comparable store sales growth (3)	2.9 %	3.2 %	5.7 %
Gross square footage at end of period (in thousands)	3,580	3,200	2,714
Average comparable store size (gross square feet) (4)	21,085	21,123	21,192
Comparable store sales per gross square foot during period (4)	$533	$535	$524

(1) Selling, general and administrative expenses included $2.1 million of leadership change related costs for the year ended January 25, 2015.

(2) Impairments and store closure costs for the year ended January 25, 2015 included approximately \$13.0 million in store closure and exit costs for the stores closed in fiscal 2014 and approximately \$9.0 million in impairment charges for certain store related assets. Impairments and store closure costs for the year ended January 26, 2014 included \$26.8 million in impairment charges related to certain real estate and store related assets. There was also an additional store closure charge of \$0.2 million to adjust the reserve for a previously closed store.

(3) Our practice is to include sales from a store in comparable store sales beginning on the first day of the sixteenth full month following the store's opening. We believe that comparability is achieved approximately 15 months after opening. When a store that is included in comparable store sales is remodeled or relocated, we continue to consider sales from that store to be comparable store sales. When a store is closed it is removed from comparable store sales in the period it is closed. There may be variations in the way that our competitors calculate comparable or "same store" sales. As a result, data in this Form 10-K regarding our comparable store sales may not be comparable to similar data made available by our competitors.

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(4) Average comparable store size and comparable store sales per gross square foot are calculated using the gross square footage and sales for stores included within our comparable store base for each month during the given period.

Percentage totals in the above table may not equal the sum of the components due to rounding.

Items Impacting Comparability

For the Year Ended January 25, 2015

- Approximately $13.5 million, or $0.18 per share on a diluted basis, for the year ended January 25, 2015 associated with the store closure and exit costs related to the locations that closed in fiscal 2014. Included in the $13.5 million is approximately $13.0 million for the recognition of certain lease liabilities, severance, loss on disposal of assets and other costs which is reflected in the "Impairments and store closure costs" line item on the Consolidated Statements of Comprehensive Income. The remaining charges relate to the liquidation of inventory and are reflected in other line items on the Consolidated Statements of Comprehensive Income.
- Approximately $9.0 million, or $0.11 per share on a diluted basis, for the year ended January 25, 2015 associated with the impairment of certain store related assets, which is reflected in the "Impairments and store closure costs" line item on the Consolidated Statements of Comprehensive Income.
- Approximately $2.1 million, or $0.03 per share on a diluted basis, for the year ended January 25, 2015 associated with the previously announced leadership change and related charges are included in the "Selling, general and administrative expenses" line item on the Consolidated Statements of Comprehensive Income.

The above items had an impact to the tax rate resulting in a reduction of approximately $0.01 per share on a diluted basis for the year ended January 25, 2015.

For the Year Ended January 26, 2014

- Approximately $27.6 million in charges, or $0.35 per share on a diluted basis, for the year ended January 26, 2014, associated with the impairment of certain real estate and store related assets. Of these charges, $27.0 million is included in the "Impairments and store closure costs" line item and $0.6 million related to the write off of capitalized expenses for real estate sites prior to leasing them is included in the "Selling, general and administrative expenses" line item on the Consolidated Statements of Comprehensive Income.

For the Year Ended January 27, 2013

- Approximately $0.5 million, or $0.01 per share on a diluted basis, for the year ended January 27, 2013, in issuance costs incurred in conjunction with our public offering of common stock, which closed on June 18, 2012. As agreed upon by and among us and certain stockholders, we were obligated to bear the expenses and fees, except for underwriting discounts and commissions. We received no proceeds in connection with the public offering, and all fees and expenses incurred during the year ended January 27, 2013 were expensed and included in the "Selling, general and administrative expenses" line item on the Consolidated Statements of Comprehensive Income.

Year Ended January 25, 2015 Compared to the Year Ended January 26, 2014

Sales

Sales increased 16.0%, or $241.5 million, to $1.75 billion for the year ended January 25, 2015, as compared to the year ended January 26, 2014. The increase in sales for the year ended January 25, 2015 was primarily attributable to sales from 22 new stores that were not open during the year ended January 26, 2014, increased sales from 19 stores that were only open during a portion of the year ended January 26, 2014 and an overall increase in comparable store sales. There were 140 comparable stores and 29 non-comparable stores open at January 25, 2015.

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Comparable store sales increased 2.9% for the year ended January 25, 2015, as compared to the year ended January 26, 2014, as a result of a 2.8% increase in the number of transactions and a 0.1% increase in the average transaction size at our comparable stores. Average customer transaction size at our comparable stores increased to $31.90 for the year ended January 25, 2015, from $31.86 for the year ended January 26, 2014.

Gross Profit

Gross profit increased 15.4%, or $79.3 million, to $594.6 million for the year ended January 25, 2015, as compared to the year ended January 26, 2014. The amount of the increase in gross profit attributable to increased sales was $82.3 million and was partially offset by a $3.0 million decrease in gross profit attributable to a decrease in the gross margin rate. Our cost of goods sold increased by $162.2 million for the year ended January 25, 2015, as compared to the year ended January 26, 2014, which was primarily attributable to a $145.0 million increase in merchandise product costs, a $12.6 million increase in store occupancy costs, a $3.2 million increase in supply expense, and a $1.0 million increase in LIFO expense. Gross margin rate decreased 20 basis points to 33.9% for the year ended January 25, 2015 from 34.1% for the year ended January 26, 2014. The reduction in our gross margin rate was primarily driven by a decrease in merchandise margins due to our decision to absorb cost inflation for certain product categories.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased 16.2%, or $56.6 million, to $406.5 million for the year ended January 25, 2015, as compared to the year ended January 26, 2014. The increase in selling, general and administrative expenses was primarily attributable to an increase in the number of stores in operation and an increase in customer traffic during the year ended January 25, 2015, as compared to the year ended January 26, 2014, which led to higher overall store-level compensation expenses as well as other costs to operate our stores. With more stores in operation during the year ended January 25, 2015, our store salary and benefit expenses increased $39.5 million and other store operating expenses increased $9.6 million, compared to the year ended January 26, 2014. In addition, corporate general and administrative expenses increased $8.4 million for the year ended January 25, 2015, as compared to the year ended January 26, 2014, which included charges of $2.1 million related to the announced leadership change in fiscal 2014. The increase in selling, general and administrative expenses was partially offset by a decrease in pre-opening expenses of $0.4 million for the year ended January 25, 2015, as compared to the year ended January 26, 2014.

As a percentage of sales, selling, general and administrative expenses for the year ended January 25, 2015 were 23.2%, or 10 basis points higher, than the selling, general and administrative expenses for the year ended January 26, 2014. The increase in selling, general and administrative expenses as a percentage of sales was primarily related to the 10 basis point increase associated with the previously announced leadership change.

Impairments and Store Closure Costs

Impairments and store closure costs for the year ended January 25, 2015 were $22.6 million, as compared to $27.5 million for the year ended January 26, 2014. Impairments and store closure costs for the year ended January 25, 2015 were primarily comprised of approximately $13.0 million in store closure and exit costs for the stores closed in fiscal 2014 and approximately $9.0 million in impairment charges for certain store related assets. Impairments and store closure costs for the year ended January 26, 2014 were primarily comprised of $26.8 million in impairment charges and $0.2 million for an adjustment to the reserve related to a previously closed store. The remaining charges for the years ended January 25, 2015 and January 26, 2014 relate to ongoing expenses associated with closed stores.

Depreciation Expense

Depreciation increased 13.4%, or $7.3 million, to $62.0 million for the year ended January 25, 2015, as compared to the year ended January 26, 2014, principally due to store unit growth and the recognition of depreciation expense for certain store locations, which are recorded as capital and financing lease assets. Depreciation expense as a percentage of sales decreased by 10 basis points to 3.5% for the year ended January 25, 2015, compared to 3.6% for the year ended January 26, 2014.

Income from Operations

For the year ended January 25, 2015, operating income increased $20.2 million, to $103.6 million from $83.4 million for the year ended January 26, 2014. For the year ended January 25, 2015, we recognized charges of approximately $24.5 million associated with store closure and exit costs, impairments of certain store related assets and charges related to a change in leadership. For the year ended January 26, 2014, we recognized charges of approximately $27.6 million associated with

impairments for certain real estate and store related assets. Excluding these items, adjusted operating income was $128.1 million for the year ended January 25, 2015, an increase of 15.5%, from adjusted operating income of $111.0 million for the year ended January 26, 2014.
Income from operations as a percentage of sales for the year ended January 25, 2015 increased to 5.9% from 5.5% for the year ended January 26, 2014. The increase in our income from operations as a percentage of sales for the year ended January 25, 2015, compared to the year ended January 26, 2014, was primarily due to a decrease in impairment charges, partially offset by a decrease in the gross margin rate, as described above. Adjusted income from operations as a percentage of sales remained flat at 7.3% for the years ended January 25, 2015 and January 26, 2014.

The following table provides an unaudited reconciliation of adjusted income from operations, a non-GAAP financial measure, to GAAP income from operations for the year ended January 25, 2015. For an unaudited reconciliation of adjusted income from operations to GAAP income from operations for the year ended January 26, 2014, see "Year Ended January 26, 2014 Compared to the Year Ended January 27, 2013" below.

	Year Ended January 25, 2015 (unaudited) (amounts in millions)
Income from operations	$103.6
Store closure and exit costs	13.5
Impairment of certain store related assets	9.0
Leadership related charges	2.1
Adjusted income from operations (1)	$128.1

(1) The adjusted income from operations total may not equal the sum of the components due to rounding.
Interest Expense

Interest expense increased 15.6%, or $0.6 million, to $4.4 million for the year ended January 25, 2015, as compared to $3.8 million for the year ended January 26, 2014. The increase was primarily attributable to an increase in interest expense related to capital and financing lease obligations, partially offset by a decrease in interest expense associated with the debt balance for the year ended January 25, 2015, compared to the year ended January 26, 2014.

Income Tax Expense

The effective income tax rate for the year ended January 25, 2015 was 36.5% as compared to 36.2% for the year ended January 26, 2014.

Net Income

Net income increased 24.0%, or $12.2 million, to $63.0 million for the year ended January 25, 2015, from $50.8 million for the year ended January 26, 2014. Net income was negatively affected by pre-tax charges of $24.5 million associated with store closure and exit costs related to the stores closed in fiscal 2014, impairment charges for certain store related assets, and costs associated with the previously announced leadership change for the year ended January 25, 2015, compared to pre-tax charges of $27.6 million associated with impairments for certain real estate and store related assets for the year ended January 26, 2014. Adjusted net income increased 15.4%, or $10.4 million, to $78.0 million, for the year ended January 25, 2015, compared to adjusted net income of $67.6 million for the year ended January 26, 2014.

Net income as a percentage of sales for the year ended January 25, 2015 increased to 3.6% from 3.4% for the year ended January 26, 2014. Adjusted net income as a percentage of sales remained flat at 4.5% for the years ended January 25, 2015 and January 26, 2014.

The following table provides an unaudited reconciliation of adjusted net income, a non-GAAP financial measure, to GAAP net income for the year ended January 25, 2015. For an unaudited reconciliation of adjusted net income to GAAP net income for the year ended January 26, 2014, see “Year Ended January 26, 2014 Compared to the Year Ended January 27, 2013” below.:

	Year Ended January 25, 2015 (unaudited) (amounts in millions, except per share amounts)	
	Adjusted Net Income	Adjusted Diluted Earnings Per Share, after tax
Net income	$63.0	$1.30
Store closure and exit costs	13.5	0.18
Impairment of certain store related assets	9.0	0.11
Leadership related charges	2.1	0.03
Tax provision (1)	(9.5)	(0.01)
Adjusted net income (2)	$78.0	$1.61

(1) Tax provision represents the additional income tax expense if the items above were excluded from the calculation of taxable income. The amounts shown for each item in the "Adjusted Diluted Earnings Per Share, after tax" column are net of the impact of the tax provision. The $0.01 shown in the "Tax provision" line of the "Adjusted Diluted Earnings Per Share, after tax" column represents the effect of the above items on the Company's tax rate, to the extent not already captured above.
(2) The adjusted net income total may not equal the sum of the components due to rounding.

Year Ended January 26, 2014 Compared to the Year Ended January 27, 2013

Sales

Sales increased 13.7%, or $182.5 million, to $1.5 billion for the year ended January 26, 2014, as compared to the year ended January 27, 2013. The increase in sales for the year ended January 26, 2014 was primarily attributable to sales from 22 stores that were not open during the year ended January 27, 2013, increased sales from 16 stores that were only open during a portion of the year ended January 27, 2013 and an overall increase in comparable store sales. There were 125 comparable stores and 26 non-comparable stores open at January 26, 2014.
Comparable store sales increased 3.2% for the year ended January 26, 2014, as compared to the year ended January 27, 2013, as a result of a 1.7% increase in the number of transactions and a 1.5% increase in the average transaction size at our comparable stores. Average customer transaction size at our comparable stores increased to $32.01 for the year ended January 26, 2014, from $31.55 for the year ended January 27, 2013.

Gross Profit

Gross profit increased 14.1%, or $63.7 million, to $515.4 million for the year ended January 26, 2014, as compared to the year ended January 27, 2013. The amount of the increase in gross profit attributable to increased sales was $62.0 million, and the amount of the increase in gross profit attributable to increased gross margin rate was $1.7 million. Our cost of goods sold increased by $118.9 million for the year ended January 26, 2014, as compared to the year ended January 27, 2013, which was primarily attributable to a $105.9 million increase in merchandise product costs and a $9.8 million increase in store occupancy costs. Gross margin rate increased 10 basis points to 34.1% for the year ended January 26, 2014 from 34.0% for the year ended January 27, 2013. The increase in our gross margin rate was primarily attributable to increased merchandise margin.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased 15.3%, or $46.3 million, to $349.8 million for the year ended January 26, 2014, as compared to the year ended January 27, 2013. The increase in selling, general and administrative expenses was primarily attributable to an increase in the number of stores in operation and an increase in customer traffic during the year ended January 26, 2014, as compared to the year ended January 27, 2013, which led to higher overall store-level compensation expenses and other costs to operate our stores. With more stores in operation during the year ended January 26, 2014, our store salary and benefit expenses increased $34.9 million, our other store operating expenses increased $6.6 million, and new store pre-opening expenses increased $2.0 million, compared to the year ended January 27, 2013. There was also a $2.7 million increase in our corporate administrative expenses for the year ended January 26, 2014, as compared to the year ended January 27, 2013, primarily attributable to employee compensation expenses due to an increase in headcount reduced by lower incentive compensation expenses. As a percentage of sales, selling, general and administrative expenses for the year ended January 26, 2014 were 23.1%, or 30 basis points, higher than the selling, general and administrative expenses for the year ended January 27, 2013. The increase in selling, general and administrative expenses as a percentage of sales was primarily the result of lower than expected sales in certain non-comparable stores combined with expense increases related to store-level compensation at some of these non-comparable stores as we provided higher service levels to build our brand in new markets and operate in markets with higher wage rates. Additionally, we incurred higher pre-opening expenses offset by reduced corporate expenses as a percentage of sales for the year ended January 26, 2014 compared to the year ended January 27, 2013.

Impairments and Store Closure Costs

Impairments and store closure costs for the year ended January 26, 2014 were primarily comprised of a $26.8 million impairment charge related to certain real estate and store related assets and include a $0.2 million adjustment for a previously closed store. We did not have any impairment charges for the year ended January 27, 2013.

Depreciation Expense

Depreciation increased 19.5%, or $8.9 million, to $54.7 million for the year ended January 26, 2014, compared to the year ended January 27, 2013, principally due to store unit growth and the recognition of depreciation expense for certain store locations, which are recorded as capital and financing lease assets. Depreciation expense as a percentage of sales increased by 20 basis points to 3.6% for the year ended January 26, 2014, compared to 3.4% for the year ended January 27, 2013.

Income from Operations

For the year ended January 26, 2014, operating income decreased $18.1 million, to $83.4 million from $101.5 million for the year ended January 27, 2013 primarily due to a $27.6 million increase in impairment charges related to certain real estate and store related assets and a $13.8 million increase in operating losses associated with activities related to stores operating in California and Texas. Excluding impairment charges, adjusted operating income was $111.0 million for the year ended January 26, 2014, an increase of 9.3% compared to the year ended January 27, 2013.

Income from operations as a percentage of sales for the year ended January 26, 2014 decreased to 5.5% from 7.6% for the year ended January 27, 2013. The decrease in our income from operations as a percentage of sales for the year ended January 26, 2014, compared to the year ended January 27, 2013, was primarily due to the 180 basis points in impairment charges, and higher selling, general and administrative and depreciation expenses, partially offset by improved gross margin, as described above. Adjusted operating income as a percentage of sales was 7.3% for the year ended January 26, 2014.

The following table provides an unaudited reconciliation of adjusted income from operations, a non-GAAP financial measure, to GAAP income from operations:

	Year Ended January 26, 2014 (unaudited) (amounts in millions)
Income from operations	$83.4
Impairment of certain real estate and store related assets	27.6
Adjusted income from operations	$111.0

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Interest Expense

Interest expense increased 152.5%, or $2.3 million, to $3.8 million for the year ended January 26, 2014, as compared to $1.5 million for the year ended January 27, 2013. The increase was primarily attributable to $3.2 million of interest expense related to capital lease and financing obligations for the year ended January 26, 2014, compared to $0.3 million of interest expense for the year ended January 27, 2013.

Income Tax Expense

The effective income tax rate for the year ended January 26, 2014 was 36.2% as compared to 35.9% for the year ended January 27, 2013.

Net Income

Net income decreased 20.8%, or $13.3 million, to $50.8 million for the year ended January 26, 2014, from $64.1 million for the year ended January 27, 2013. Net income was negatively affected by a $27.6 million pre-tax impairment charge for the year ended January 26, 2014. Net income as a percentage of sales for the year ended January 26, 2014 decreased to 3.4% from 4.8% for the year ended January 27, 2013. Adjusted net income was $67.6 million, or 4.5% as a percentage of sales, for the year ended January 26, 2014.

The following table provides an unaudited reconciliation of adjusted net income, a non-GAAP financial measure, to GAAP net income:

	Year Ended January 26, 2014 (unaudited) (amounts in millions, except per share amounts)	
	Adjusted Net Income	Adjusted Diluted Earnings Per Share, after tax
Net income	$50.8	$1.05
Impairment of certain real estate and store related assets	27.6	0.36
Tax provision (1)	(10.8)	(0.01)
Adjusted net income	$67.6	$1.40

(1) Tax provision represents the additional income tax expense if the items above were excluded from the calculation of taxable income. The amounts shown for each item in the "Adjusted Diluted Earnings Per Share, after tax" column are net of the impact of the tax provision. The $0.01 shown in the "Tax provision" line of the "Adjusted Diluted Earnings Per Share, after tax" column represents the effect of the above items on the Company's tax rate, to the extent not already captured above.

Liquidity and Capital Resources

Our primary sources of liquidity are cash generated from operations and borrowings under our revolving credit facility. Our primary uses of cash are purchases of inventory, operating expenses, capital expenditures primarily for opening new stores and relocating and remodeling existing stores, debt service, and corporate taxes. We believe that the cash generated from operations, together with the borrowing availability under our revolving credit facility, will be sufficient to meet our working capital needs for at least the next twelve months, including investments made, and expenses incurred, in connection with opening new stores and relocating and remodeling existing stores and other strategic initiatives. These strategic initiatives include the replacement of store equipment and product display fixtures, and investments in information technology and merchandising enhancements. Our working capital position benefits from the fact that we generally collect cash from sales to customers the same day or, in the case of credit or debit card transactions, within a few business days of the related sale.

At January 25, 2015, we had $48.5 million in cash and cash equivalents and $149.6 million in borrowing availability pursuant to our revolving credit facility. Our revolving credit facility is discussed under "—Financing Activities" and "—Revolving Credit Facility" below.

While we believe we have sufficient liquidity and capital resources to meet our current operating requirements and expansion plans, we may elect to pursue additional expansion opportunities within the next year which could require additional debt or equity financing. If we are unable to secure additional financing at favorable terms in order to pursue such additional expansion opportunities, our ability to pursue such opportunities could be materially adversely affected.

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

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
	(in thousands)		
Net cash provided by operating activities	$143,025	$140,372	$109,118
Net cash used in investing activities	(82,178)	(122,247)	(91,613)
Net cash used in financing activities	(24,106)	(15,117)	(19,449)
Net increase (decrease) in cash and cash equivalents	$36,741	$3,008	$(1,944)

Operating Activities

Cash provided by operating activities consists primarily of net income adjusted for non-cash items, including depreciation and amortization, realized losses on disposal of property and equipment, impairment charges, share-based compensation, changes in deferred taxes, and the effect of changes in assets and liabilities.

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
	(in thousands)		
Net income	$63,025	$50,807	$64,133
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	62,163	54,878	45,962
Loss on disposals of property and equipment	2,006	311	170
Impairment of property and equipment	8,961	26,828	—
Gain on assignment of capital lease	(1,508)	—	—
Share-based compensation	7,533	5,239	4,259
Excess tax benefits from share-based compensation	(324)	(569)	(1,140)
Deferred income taxes	(16,230)	(11,519)	(6,339)
Changes in assets and liabilities	17,399	14,397	2,073

Net cash provided by operating activities	$143,025	$140,372	$109,118

Net cash provided by operating activities increased 1.9% or $2.7 million, to $143.0 million for the year ended January 25, 2015, compared to $140.4 million for the year ended January 26, 2014 primarily attributable to higher net income before impairments and store closure and exit costs, partially offset by a use of working capital.

Net cash provided by operating activities increased 28.6%, or $31.3 million, to $140.4 million for the year ended January 26, 2014, compared to $109.1 million for the year ended January 27, 2013 primarily attributable to higher net income before impairments and improved working capital.

Investing Activities

Cash used in investing activities consists primarily of capital expenditures for opening new stores and relocating and remodeling existing stores, as well as investments in information technology and merchandising enhancements.

	Year Ended		
	January 25, 2015	January 26, 2014	January 27, 2013
	(in thousands)		
Purchases of property and equipment	$(90,182)	$(122,366)	$(81,107)
Proceeds from sale of property and equipment	8,004	119	6,698
Payments for lease acquisition costs	—	—	(17,204)
Net cash used in investing activities	$(82,178)	$(122,247)	$(91,613)

Capital expenditures decreased $32.2 million to $90.2 million for the year ended January 25, 2015, as compared to $122.4 million for the year ended January 26, 2014. The decrease in capital expenditures was primarily related to a reduced average cost of new store construction and a decrease in the number of stores remodeled and under construction for the year ended January 25, 2015. Capital expenditures related to real estate activities were 83.5% and 91.8% of the total capital expenditures for the years ended January 25, 2015 and January 26, 2014, respectively. During the year ended January 25, 2015, we opened 22 new stores. In November 2014, we received proceeds of $7.9 million from a land and building sale-leaseback transaction.

Capital expenditures increased $41.3 million to $122.4 million for the year ended January 26, 2014, compared to $81.1 million for the year ended January 27, 2013. The increase in capital expenditures was primarily related to an increase in new store growth for the year ended January 26, 2014. Capital expenditures related to real estate activities were 91.8% and 85.3% of the total for the years ended January 26, 2014 and January 27, 2013, respectively. During the year ended January 26, 2014, we opened 22 new stores and remodeled 3 stores. Additionally, the increase in new store capital expenditures was related to higher than normal spending on certain projects. Our new store capital expenditures also included the construction of several buildings, versus our typical leasehold improvements. In April 2012, we received proceeds of $6.6 million from a land and building sale-leaseback transaction.

We plan to spend approximately $100.0 million to $110.0 million on capital expenditures during fiscal 2015, primarily related to real estate investments as we plan to refresh or remodel ten stores and construct and open 19 new stores in fiscal 2015.

Financing Activities

Cash used in financing activities consists principally of borrowings and payments under our revolving credit facility.

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
	(in thousands)		
Borrowings on revolving credit facility	$138,233	$513,621	$466,324
Payments made on revolving credit facility	(162,933)	(530,921)	(488,324)
Payments made for debt issuance costs	(534)	—	—
Payments made on capital and financing lease obligations	(836)	(177)	—
Proceeds from issuance of common stock pursuant to employee stock purchase plan	170	226	185
Excess tax benefits from share-based compensation	324	569	1,140
Payments made on withholding tax for restricted stock unit vesting	(468)	(494)	(492)
Proceeds from exercise of share-based compensation awards	1,938	2,059	1,718
Net cash used in financing activities	$(24,106)	$(15,117)	$(19,449)

Net cash used in financing activities during the year ended January 25, 2015 increased $9.0 million, to $24.1 million, from the year ended January 26, 2014, mostly due to an increase in net payments on our revolving credit facility. We reduced our credit facility balance by $24.7 million for the year ended January 25, 2015, compared to $17.3 million for the year ended January 26, 2014.

Net cash used in financing activities during the years ended January 26, 2014 and January 27, 2013 was $15.1 million and $19.5 million, respectively. Net repayments under our revolving credit facility were $17.3 million for the year ended January 26, 2014, compared to $22.0 million for the year ended January 27, 2013.

Revolving Credit Facility

On June 12, 2014, we entered into an unsecured revolving credit agreement with Bank of America, N.A., as Administrative Agent, Swing Line Lender and Letter of Credit Issuer, and the several lenders party thereto (the “2014 Credit Agreement”). The 2014 Credit Agreement refinanced and replaced our senior unsecured revolving credit facility under that certain Credit Agreement, dated February 22, 2011, with Bank of America, N.A., as Administrative Agent, Swing Line Lender and Letter of Credit Issuer, and the several lenders party thereto (the “2011 Credit Agreement”). The 2011 Credit Agreement was terminated effective June 12, 2014 upon our entering into the 2014 Credit Agreement.
The 2014 Credit Agreement matures June 12, 2019 and is available to provide support for working capital, capital expenditures and other general corporate purposes, including permitted acquisitions and issuance of letters of credit. While we currently have no material domestic subsidiaries, other entities will guarantee our

obligations under the 2014 Credit Agreement if and when they become our material domestic subsidiaries during the term of the 2014 Credit Agreement.

The 2014 Credit Agreement provides for total borrowings of up to $175 million. Under the terms of the 2014 Credit Agreement, we are entitled to request an increase in the size of the facility by an amount not exceeding $100 million in the aggregate. If the existing lenders elect not to provide the full amount of a requested increase, or in lieu of accepting offers from existing lenders to increase their commitments, we may designate one or more other lenders to become a party to the 2014 Credit Agreement, subject to the approval of the Administrative Agent. The 2014 Credit Agreement includes a letter of credit sublimit of $60 million and a swing line sublimit of $15 million.

At our option, revolving loans under the 2014 Credit Agreement bear interest at (i) the London Interbank Offered Rate ("LIBOR") plus an applicable margin that ranges from 0.90% to 2.00%, (ii) the Eurodollar rate plus an applicable margin that ranges from 0.90% to 2.00%, or (iii) the base rate plus an applicable margin that ranges from 0% to 1.00%, where the base rate is defined as the greatest of: (a) the federal funds rate plus 0.50%, (b) Bank of America’s prime rate, and (c) the Eurodollar rate plus 1.00%. As of January 25, 2015, there were no outstanding borrowings under the 2014 Credit Agreement.

The commitment fee calculated on the unused portions of the 2014 Credit Agreement ranges from 0.125% to 0.250% per annum.

The 2014 Credit Agreement contains a number of affirmative and restrictive covenants, including limitations on our ability to grant liens, incur additional debt, pay dividends, redeem our common stock, make certain investments and engage in certain merger, consolidation or asset sale transactions.

In addition, the 2014 Credit Agreement provides that we are required to maintain the following financial ratios:

- a consolidated maximum leverage ratio as of the end of any fiscal quarter of not more than 4.25 to 1.00, based upon the ratio of (i) Adjusted Funded Debt (as defined in the 2014 Credit Agreement) minus certain cash and cash equivalents in excess of $5.0 million as of the end of each fiscal quarter to (ii) Consolidated EBITDAR (as defined in the 2014 Credit Agreement) for the period consisting of the four fiscal quarters then ending; and
- a consolidated fixed charge coverage ratio as of the end of each fiscal quarter of not less than 1.70 to 1.00, based upon the ratio of (i) Consolidated EBITDAR less cash taxes paid and dividends and other distributions made in respect of capital stock, in each case, over the period consisting of the four fiscal quarters then ending to (ii) the sum of cash interest, lease, rent and scheduled principal payments on Funded Debt (as defined in the 2014 Credit Agreement), in each case, over the period consisting of the four fiscal quarters then ending.

The 2014 Credit Agreement contains customary events of default. If an Event of Default (as defined in the 2014 Credit Agreement) occurs and is continuing, on the terms and subject to the conditions set forth in the 2014 Credit Agreement, amounts outstanding under the 2014 Credit Agreement may be accelerated and may become or be declared immediately due and payable.

We were in compliance with all debt covenants under the 2014 Credit Agreement as of January 25, 2015.

Contractual Obligations

The following table summarizes our contractual obligations, as of January 25, 2015.

	Payments Due by Period (in thousands)				
Contractual obligations	Total	Less than 1 year	1 - 3 years	3 - 5 years	More than 5 years
Estimated interest on long-term debt obligations (1)	$1,728	$416	$768	$544	$—
Operating lease obligations (2)	525,175	56,450	117,713	110,962	240,050
Capital and financing lease obligations, including principal and interest payments (3)	70,146	5,040	10,432	10,468	44,206
Purchase obligations (4)	4,388	4,388	—	—	—
Contractual obligations for construction-related activities	10,142	10,142	—	—	—
	$611,579	$76,436	$128,913	$121,974	$284,256

(1) The outstanding advances under the 2014 Credit Agreement bear variable interest at one-month LIBOR plus an applicable margin, with a total stated interest rate of 1.1% at January 25, 2015. For purposes of this table, we estimated interest expense (including commitments fees on the unused balance) to be paid during the remaining term of the 2014 Credit Agreement using the unused commitment fees and interest rate as of January 25, 2015. Our actual cash payments for interest under the 2014 Credit Agreement will fluctuate as the outstanding balance changes with our cash needs and the one-month LIBOR rate fluctuates. For a more detailed description of the interest requirement for our long-term debt, see Note 3 to our consolidated financial statements found elsewhere in this document.

(2) Represents the minimum lease payments due under our operating leases, excluding common area maintenance, insurance and taxes related to our operating lease obligations, which combined represented approximately $14.6 million for the year ended January 25, 2015. For a more detailed description of our operating leases, see Note 6 to our consolidated financial statements found elsewhere in this Form 10-K.

(3) Represents the payments due under our capital and financing lease obligations. We do not record rent expense for these capital and financing lease obligations, but rather rental payments are recognized as a reduction of the capital and financing lease obligations and interest expense.

(4) Purchase obligations include agreements to purchase goods and services made in the normal course of business that are enforceable and legally binding on us. Our purchase obligations consist predominantly of contracts to purchase certain inventory items. This amount does not include any payment obligations with respect to products on hand at our logistics providers as we do not typically take title or have any obligation to pay for products purchased by our logistics providers until we receive the products at our store locations. Although we occasionally have obligations to purchase any inventory on-hand in the event a contract with a logistics provider is terminated, we also generally enter into arrangements with any subsequent logistics provider or distributor pursuant to which the subsequent logistics provider or distributor purchases the inventory on-hand at the former logistics provider or distributor or we deplete the inventory on-hand at the former logistics provider or distributor as the termination date approaches.

We periodically make other commitments and become subject to other contractual obligations that we believe to be routine in nature and incidental to the operation of our business. We believe that such routine commitments and contractual obligations do not have a material impact on our business, financial condition or results of operations.

Off-Balance Sheet Arrangements

Our off-balance sheet arrangements at January 25, 2015 consist of outstanding standby letters of credit discussed in Note 3 to our consolidated financial statements found elsewhere in this Form 10-K and of operating leases. We have no other off-balance sheet arrangements that have had, or are reasonably likely to have, a material current or future effect on our consolidated financial statements or changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Critical Accounting Policies

In presenting our consolidated financial statements in conformity with U.S. generally accepted accounting principles, or GAAP, we are required to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses and related disclosures.

Some of the estimates and assumptions that we are required to make relate to matters that are inherently uncertain as they pertain to future events. We base these estimates and assumptions on historical experience or on various other factors that we believe to be reasonable and appropriate under the circumstances. On an ongoing basis, we reconsider and evaluate our estimates and assumptions. Actual results may differ significantly from these estimates. Future results may differ from our estimates under different assumptions or conditions.

We believe that the critical accounting policies listed below involve our more significant judgments, assumptions and estimates and, therefore, could have the greatest potential impact on our consolidated financial statements.

For further information on our critical and other significant accounting policies, see the notes to our consolidated financial statements included elsewhere in this Form 10-K.

Leases

The most significant estimates used by management in accounting for leases and the impact of these estimates are as follows:

Expected lease term - Our expected lease term includes both contractual lease periods and cancelable option periods where failure to exercise such options would result in an economic penalty. The expected lease term is used in determining whether the lease is accounted for as an operating lease or a capital lease. A lease is considered a capital lease if the lease term exceeds 75% of the leased asset's useful life. The expected lease term is also used in determining the depreciable life of the asset. An increase in the expected lease term will increase the probability that a lease may be considered a capital lease and will generally result in higher interest and depreciation expense for a leased property recorded on our balance sheet.

Incremental borrowing rate - The incremental borrowing rate is primarily used in determining whether the lease is accounted for as an operating lease or a capital lease. A lease is considered a capital lease if the net present value of the minimum lease payments is greater than 90% of the fair market value of the property. An increase in the incremental borrowing rate decreases the net present value of the minimum lease payments and reduces the probability that a lease will be considered a capital lease. For leases which are recorded on our balance sheet with a related capital lease, the incremental borrowing rate is also used in allocating our rental payments between interest expense and a reduction of the outstanding obligation. If our calculation of the net present value of minimum lease payments is greater than the fair value of the leased asset, the incremental borrowing rate is adjusted so the net present value of the minimum lease payments does not exceed the fair value of the leased asset.

Fair market value of leased asset - The fair market value of leased retail property is generally estimated based on comparable market data as provided by third-party sources. Fair market value is used in determining whether the lease is accounted for as an operating lease or a capital lease. A lease is considered a capital lease if the net present value of the minimum lease payments equals or exceeds 90% of the fair market value of the leased property. A higher fair market value reduces the likelihood that a lease will be considered a capital lease.

Accounting owner - With certain leases, we are involved with the construction of the building and we are considered the owner of the building for accounting purposes. We capitalize the amount of total project costs incurred during the construction period as "Construction in progress." At the completion of the construction project, we evaluate whether the transfer to the landlord meets the requirements for sale-leaseback accounting treatment. A sale and leaseback of the asset is deemed to occur when construction of the asset is complete and the lease term begins and the relevant sale-leaseback accounting criteria are met. Any gain or loss from the transaction is deferred and amortized as rent expense on a straight-line basis over the term of the lease. If we do not pass the criteria for sale-leaseback accounting, we record a financing lease asset as a building, which is included in the "Property and equipment, net" line item and a corresponding financing obligation in the “Capital and financing lease obligations” line item on our Consolidated Balance Sheets. We allocate each lease payment between a reduction of the lease obligation and interest expense using the effective interest method.

Inventories

Our inventories are stated at the lower of cost or market. Predominantly all of our inventories are valued using the last-in, first-out, or LIFO, method whereby the costs of the first items purchased remain in inventory and are used to value ending inventory. We use the link chain method for computing dollar value LIFO, whereby the base year values of beginning and ending inventories are determined using cumulative price indexes published by the Bureau of Labor Statistics. Valuing inventory using LIFO requires management to select from different available methods. Using a different method could result in a change in our estimate of the LIFO value of our inventory and that difference could be materially different.

We determine the current cost of our inventories using the first-in, first-out, or FIFO method. The FIFO value of inventories includes cost of goods and freight, net of vendor rebates and discounts. The excess of the current cost of inventories over the LIFO value, or the LIFO reserve, was approximately $7.7 million at January 25, 2015 and $6.7 million at January 26, 2014.

Impairment of Long-Lived Assets

We assess our long-lived assets, principally property and equipment, for possible impairment whenever events or changes in circumstances indicate the carrying value of a long-lived asset or group of assets may not be recoverable. Impairment evaluations for individual stores take into consideration a store’s operating cash flows, the period of time the store has been opened, and management's expectations of operating performance. Recoverability is measured by a comparison of the carrying amount of the assets to the future undiscounted cash flows expected to be generated by the assets. If impairment is indicated, a loss is recognized for any excess of the carrying value over the estimated fair value of the asset.

Our judgment regarding the existence of circumstances that indicate an asset’s carrying value may not be recoverable, and therefore potentially impaired, is based on several factors, including a decision to close a store or negative operating cash flows. Determining whether impairment exists requires that we use estimates and assumptions of projected cash flows and operating results for the asset or assets being assessed. Our cash flow projections look several years into the future and include assumptions concerning variables such as the potential impact of operational changes, competitive factors, inflation and the economy. Our estimate of fair value used in calculating an impairment loss is based on market values, if available, or our estimated future cash flow projections discounted to their present value, which are considered Level 3 inputs. Using different assumptions could result in a change in our estimates of cash flows and fair value and those differences could produce materially different results.

Closed Store Reserves

We record a reserve for future lease obligations associated with stores that are no longer being utilized in our current operations. The fair value of the closed store liability is estimated using a discount rate to calculate the present value of the remaining noncancelable lease payments at the cease use date for the store, net of an estimate of subtenant income. Lease payments for operating leases included in our closed store reserve are expected to be paid over the remaining terms of the respective leases.

Our assumptions about future cash payments to be made as part of the lease agreements are based on the terms contained in the lease agreement. In determining the fair value of the liability, we offset the future lease payments with an estimate of the amount of subtenant income that could be reasonably obtained for the store properties. Our expectations of potential subtenant income are based on variable factors, including our knowledge of the geographical area in which the closed property is located and existing economic conditions. We also seek advice from local brokers and agents, commercial market value analysts, and third party fair value reports to develop our assumptions. While we believe our current estimates of reserves for closed properties are adequate, it is possible that market and economic conditions could cause us to change our assumptions and may require additional reserves. We review our estimates used in determining the closed store reserve on a quarterly basis and record adjustments, if necessary, in the period in which the change becomes known.

Insurance Reserves

We use a combination of insurance and self-insurance to provide for potential liability for workers’ compensation, automobile and general liability, product liability, directors' and officers’ liability, employee health care benefits, and other casualty and property risks. Liabilities associated with the risks that are retained by us are estimated, in part, by considering historical claims experience, demographic factors, severity factors and other actuarial assumptions. While we believe that our assumptions are appropriate, the estimated accruals for these liabilities could be significantly affected if future occurrences and claims differ from these assumptions and historical trends.

Because of the significance of the judgments and estimation processes, it is likely that materially different amounts could be recorded if we used different assumptions or if the underlying circumstances were to change. A 10% change in our insurance liabilities at January 25, 2015 would have affected our annual operating income by approximately $2.0 million.

Income Taxes

We must make certain estimates and judgments in determining income tax expense for financial statement purposes. The amount of taxes currently payable or refundable is accrued, and deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

Deferred tax assets are also recognized for realizable loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the fiscal year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities for a change in tax rates is recognized in income in the period that includes the enactment date.

We apply the provisions of the authoritative guidance on accounting for uncertainty in income taxes that was issued by the Financial Accounting Standards Board, or FASB. Pursuant to this guidance, we may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities based on the technical merits of the position. The tax benefits recognized in the consolidated financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The authoritative guidance also addresses other items related to uncertainty in income taxes including derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition.

Share-based Compensation – 2010 Omnibus Incentive Compensation Plan

We grant options to purchase common stock under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, which was adopted and approved by the Board of Directors during 2010. The 2010 Omnibus Incentive Compensation Plan provides for the grant of options intended to qualify as incentive stock options, nonqualified stock options (“NSOs”), stock appreciation rights, restricted stock awards, restricted stock units, performance compensation awards, cash incentive awards, deferred share units and other equity-based and equity-related awards.

In accordance with ASC 718, Compensation–Stock Compensation, the fair value of each NSO award is estimated on the grant date using the Black-Scholes option-pricing model which requires the input of certain assumptions, including the expected life of the share-based award, stock price volatility, dividend yield and interest rate. Because there is limited history for our common stock, the expected life and volatility are based on historical data of publicly traded companies with characteristics similar to ours, such as plan design, industry, stage of life cycle and size, which we consider as part of a peer group that we use for the purposes of the Black-Scholes option-pricing model. Expected life is based on the median expected term of the peer group as disclosed in their publicly available financial statements. Volatility is calculated by taking the weighted-average of the historical volatilities of the peer group. Since our initial public offering we have not declared dividends and we do not plan to pay any dividends in the future. The risk-free rate for periods in the expected life of the option is based on the U.S. Treasury constant maturities in effect at the time of the grant.

We recognize the estimated fair value of performance-based awards as share-based compensation expense over the performance period based upon our determination of whether it is probable that the performance targets will be achieved. We assess the probability of achieving the performance targets at the end of each reporting period. Cumulative adjustments, if any, are recorded quarterly to reflect subsequent changes in the estimated outcome of performance-related conditions. The fair value of the performance-based awards is based on the fair market value of our common stock on the date of grant.

Recent Accounting Pronouncements

There were no new accounting pronouncements that we expect to have a material impact on our financial condition or results of operations in future periods.

Disclaimer on Forward-Looking Statements

Except for the historical information contained herein, the matters discussed in this analysis are forward-looking statements that involve risks and uncertainties, including but not limited to general business conditions, the timely development and successful opening and operation of new stores, the integration of acquired stores, the impact of competition and changes in government regulation. For a discussion of these and other risks and uncertainties that may affect our business, see “Cautionary Note Regarding Forward-Looking Statements” and “Item 1A. Risk Factors.” We do not undertake any obligation to update forward-looking statements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

We are exposed to interest rate changes of our long-term debt. We do not use financial instruments for trading or other speculative purposes.

Interest Rate Risk

Our principal exposure to market risk relates to changes in interest rates on borrowings under our revolving credit facility. Our revolving credit facility carries floating interest rates that are tied to LIBOR, Eurodollar, the federal funds rate or the base rate, and therefore, our statements of income and our cash flows will be exposed to changes in interest rates to the extent that we do not have effective hedging arrangements in place. Based upon a sensitivity analysis at January 25, 2015, a hypothetical 1.0% change in interest rates would not change our annual interest expense as a result of our zero debt balance. We do not use derivative financial instruments for speculative or trading purposes; however, this does not preclude our adoption of specific hedging strategies in the future.

Item 8. Financial Statements and Supplementary Data.

Our consolidated financial statements and related notes begin on page F-1, which are included in this Form 10-K.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

There are no changes in accountants or disagreements with accountants on accounting principles and financial disclosures required to be disclosed in this Item.

Item 9A. Controls and Procedures.

Conclusion Regarding Disclosure Controls and Procedures

We maintain disclosure controls and procedures designed to provide reasonable assurance to achieve the objective that information in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified and pursuant to the regulations of the SEC. Disclosure controls and procedures, as defined in Rule 13a-15(e) and Rule 15d-15(e) under the Exchange Act, include controls and procedures designed to ensure the information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to our management, including the Interim Chief Executive Officer and President and the Executive Vice President and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. It should be noted that our system of controls and procedures, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system are met.

As required by Rule 13a-15(b) under the Exchange Act, we carried out an evaluation, under the supervision and with participation of our management, including the Interim Chief Executive Officer and President and the Executive Vice President and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of January 25, 2015, the end of the period covered by this report.

Based on the evaluation, our Interim Chief Executive Officer and President and our Executive Vice President and Chief Financial Officer have concluded that our disclosure controls and procedures were effective at a reasonable assurance level as of January 25, 2015.

Management’s Annual Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Exchange Act Rule 13a-15(f). Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and preparation of consolidated financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that:

(i) pertain to the maintenance of records that, in a reasonable detail, accurately and fairly reflect the dispositions of our transactions and assets;

(ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

(iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisitions, use or disposition of our assets that could have a material adverse effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We have assessed the effectiveness of our internal control over financial reporting as of January 25, 2015 using the criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

Based on our assessment of the design and related testing of the internal control over financial reporting, management has concluded that, as of January 25, 2015, we have maintained effective internal control over financial reporting based on the criteria set forth in the COSO framework.

Our independent auditors, Ernst & Young LLP, a registered public accounting firm, are appointed by the Audit Committee of our Board of Directors. Ernst & Young LLP has audited and reported on our consolidated financial statements and our internal control over financial reporting. The reports of the independent auditors are contained in this Annual Report.

The effectiveness of our internal control over financial reporting has been audited by our independent auditor, Ernst & Young LLP, a registered public accounting firm, as stated in their report at page F-2 herein.

Changes in Internal Control Over Financial Reporting

There has been no change during the quarter ended January 25, 2015 in the Company’s internal control over financial reporting that was identified in connection with the evaluation required by Exchange Act Rule 13a-15(d) which has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

As noted above, management has concluded that our disclosure controls and procedures were effective as of January 25, 2015.

Item 9B. Other Information

Not applicable.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

The Company will file with the SEC a definitive proxy statement, which we refer to as the Proxy Statement, no later than 120 days after the close of its fiscal year ended January 25, 2015. The information required by this Item and not given in this Item will appear under the headings "Election of Directors," “Corporate Governance,” “Executive Officers,” and “Section 16(a) Beneficial Ownership Reporting Compliance,” in the Proxy Statement, which sections are incorporated in this Item by reference.

We have adopted a written code of conduct, which is intended to qualify as a “code of ethics” within the meaning of Item 406 of Regulation S-K of the Exchange Act, which we refer to as our Code of Ethics for Financial and Executive Officers (the “Code”). The Code applies to our principal executive officer, principal financial officer, principal accounting officer and persons performing similar functions. The Code is available on our website at www.thefreshmarket.com. We will disclose information pertaining to amendments or waivers to provisions of the Code that apply to our principal executive officer, principal financial officer, principal accounting officer or persons performing similar functions and that relate to the elements of the Code enumerated in the SEC rules and regulations by posting this information on our website at www.thefreshmarket.com. The information on our website is not a part of this Form 10-K and is not incorporated by reference in this report or any of our other filings with the SEC.

Item 11. Executive Compensation.

The information required by this Item will appear under the headings “Compensation Discussion and Analysis,” “Executive Compensation Tables,” “Compensation Committee Interlocks and Insider Participation,” “Compensation Committee Report” and “Director Compensation” in the Proxy Statement, which sections are incorporated in this Item by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information required by this Item will appear under the headings "Security Ownership of Certain Beneficial Owners and Management" and “Equity Compensation Plan Information” in the Proxy Statement, which sections are incorporated in this Item by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by this Item will appear under the headings “Corporate Governance-Policy for Review of Related Person Transactions,” “Corporate Governance-Related Person Transactions” and “Corporate Governance-Director Independence” in the Proxy Statement, which sections are incorporated in this Item by reference.

Item 14. Principal Accountant Fees and Services.

The information required by this Item will appear under the heading “Ratification of the Appointment of Independent Registered Public Accounting Firm” in the Proxy Statement, which section is incorporated in this Item by reference.

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PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) The following documents are filed as part of this report:

(1) Financial Statements: See Item 8. Financial Statements and Supplementary Data.
(2) Financial Statement Schedules: No schedules are required.
(3) Exhibits are incorporated herein by reference or are filed with this report as indicated below.

(b) Exhibits

Exhibit Number	Description
3.1	Certificate of Incorporation of The Fresh Market, Inc., incorporated by reference to Exhibit 3.1 to Form 10-K filed March 22, 2011.
3.2	Amended and Restated Bylaws of The Fresh Market, Inc., incorporated by reference to Exhibit 3.2 to Form 10-K filed March 22, 2011.
4.1	Specimen Common Stock Certificate, incorporated by reference to Exhibit 4.1 to Form S-1/A filed June 23, 2010.
4.2	Registration Rights Agreement, incorporated by reference to Exhibit 4.2 to Form 10-K filed March 22, 2011.
10.1+	Supply and Service Agreement, dated as of January 26, 2007, by and between The Fresh Market, Inc. and Burris Logistics, incorporated by reference to Exhibit 10.1 to Form S-1 filed May 3, 2010.
10.2+	Renewal Agreement, dated as of October 28, 2011, by and between The Fresh Market, Inc. and Burris Logistics, incorporated by reference to Exhibit 10.2 to Form 10-Q filed December 8, 2011.
10.3+	Letter Agreement, dated May 4, 2012, between The Fresh Market, Inc. and Burris Logistics, incorporated by reference to Exhibit 10.1 to Form 10-Q filed June 7, 2012.
10.4	Credit Agreement, dated as of February 22, 2011, among The Fresh Market, Inc., as borrower, Bank of America, N.A., as administrative agent, swing line lender and letter of credit issuer, and the other lenders party thereto, incorporated by reference to Exhibit 10.2 to Form S-1 filed March 23, 2011.
10.5	First Amendment to Credit Agreement, dated November 5, 2012, among The Fresh Market, Inc., as borrower, Bank of America, N.A., as administrative agent, swing line lender and letter of credit issuer, and the other lenders party thereto, incorporated by reference to Exhibit 10.5 to Form 10-K filed March 21, 2014.
10.6	Credit Agreement, dated as of June 12, 2014, among The Fresh Market, Inc., as borrower, Bank of America, N.A., as administrative agent, swing line lender and letter of credit issuer, and the other lenders party thereto, incorporated by reference to Exhibit 10.1 to Form 10-Q filed September 4, 2014.
10.7	First Amendment to Credit Agreement, dated March 13, 2015, among The Fresh Market, Inc., as borrower, Bank of America, N.A., as administrative agent, swing line lender and letter of credit issuer, and the

	other lenders party thereto. (1)
10.8	Tax Indemnification Agreement, incorporated by reference to Exhibit 10.5 to Form 10-K filed March 22, 2011.
10.9*	The Fresh Market Deferred Compensation Plan Amended and Restated Effective March 1, 2010, incorporated by reference to Exhibit 10.8 to Form S-1/A filed June 4, 2010.
10.10*	The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, incorporated by reference to Exhibit 10.10 to Form 10-K filed March 22, 2011.
10.11*	The Fresh Market, Inc. Employee Stock Purchase Plan, incorporated by reference to Exhibit 10.11 to Form 10-K filed March 22, 2011.
10.12*	The Fresh Market, Inc. Severance Plan, incorporated by reference to Exhibit 10.12 to Form S-1/A filed October 19, 2010.
10.13*	Form of Employment Agreement, incorporated by reference to Exhibit 10.13 to Form S-1/A filed October 19, 2010.
10.14*	Terms of Employment of Jeffrey C. Ackerman, incorporated by reference to Exhibit 10.1 to Form 10-Q filed September 6, 2013.

10.15*	Terms of Employment of Randall A. Young, incorporated by reference to Exhibit 10.1 to Form 10-Q filed November 26, 2013.
10.16*	Form of Option Award Agreement used for awards, if any, granted prior to January 29, 2012, incorporated by reference to Exhibit 10.14 to Form S-1/A filed October 19, 2010.
10.17*	Form of Restricted Stock Award Agreement for Non-Employee Directors, incorporated by reference to Exhibit 10.17 to Form S-1/A filed October 19, 2010.
10.18*	Form of Deferred Stock Unit Award Agreement for Non-Employee Directors under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, incorporated by reference to Exhibit 10.16 to Form 10-K filed March 27, 2013.
10.19*	Form of Director Indemnification Agreement, incorporated by reference to Exhibit 10.20 to Form S-1/A filed October 19, 2010.
10.20*	Form of Performance Share Unit Award Agreement under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, incorporated by reference to Exhibit 10.1 to Form 8-K filed March 20, 2013.
10.21*	Form of Option Award Agreement under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, incorporated by reference to Exhibit 10.2 to Form 8-K filed March 21, 2012.
10.22*	Form of Restricted Stock Award Agreement under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, incorporated by reference to Exhibit 10.3 to Form 8-K filed March 21, 2012.
10.23*	Form of Restricted Stock Unit Award Agreement under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan, incorporated by reference to Exhibit 10.4 to Form 8-K filed March 21, 2012.
10.24*	Form of The Fresh Market, Inc. Annual Incentive Compensation Program for Executive Officers for fiscal years prior to fiscal 2015, incorporated by reference to Exhibit 10.1 to Form 8-K filed March 26, 2014.
10.25*	Form of The Fresh Market, Inc. Annual Incentive Compensation Program for Executive Officers for fiscal years 2015 and later, incorporated by reference to Exhibit 10.1 to Form 8-K filed March 19, 2015.
10.26*	Form of Retention Bonus Award Agreement, incorporated by reference to Exhibit 10.1 to Form 8-K filed January 16, 2015.
10.27*	Separation Agreement, dated January 26, 2015, by and between Craig Carlock and The Fresh Market, Inc., incorporated by reference to Exhibit 10.1 to Form 8-K filed January 29, 2015.
23.1	Consent of Ernst & Young LLP. (1)
31.1	Certification Statement of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (1)
31.2	Certification Statement of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. (1)
32.1	Certification Statement of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)
32.2	Certification Statement of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (1)
101	The following financial information from The Fresh Market, Inc.'s Annual Report on Form 10-K, for the period ended January 25, 2015

formatted in eXtensible Business Reporting Language: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Consolidated Financial Statements. (1) (2)

+ Confidential treatment has been granted for certain portions which are omitted in the copy of the exhibit electronically filed with the SEC.

* Indicates a management contract or compensatory plan or arrangement.

(1) Filed herewith.

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

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE FRESH MARKET, INC.

	By: /s/ Jeffrey C. Ackerman Jeffrey C. Ackerman Executive Vice President and Chief Financial Officer
Dated: March 20, 2015	(Principal Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on March 20, 2015.

Name	Title
/s/ Sean Crane Sean Crane	Interim Chief Executive Officer and President (Principal Executive Officer)
/s/ Jeffrey C. Ackerman Jeffrey C. Ackerman	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
/s/ Jeffrey B. Short Jeffrey B. Short	Vice President and Controller (Principal Accounting Officer)
/s/ Jeffrey Naylor Jeffrey Naylor	Director
/s/ Richard Noll Richard Noll	Director
/s/ Bob Sasser Bob Sasser	Director
/s/ Steven Tanger Steven Tanger	Director
/s/ Jane Thompson Jane Thompson	Director
/s/ Michael Tucci	

Michael Tucci	Director

The Fresh Market, Inc.

Consolidated Financial Statements

For the Years Ended January 25, 2015, January 26, 2014, and January 27, 2013

Index to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting

The Board of Directors and Stockholders of
The Fresh Market, Inc.

We have audited The Fresh Market, Inc's. internal control over financial reporting as of January 25, 2015, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). The Fresh Market, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, The Fresh Market, Inc. maintained, in all material respects, effective internal control over financial reporting as of January 25, 2015, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of The Fresh Market, Inc. as of January 25, 2015 and January 26, 2014, and the related consolidated statements of comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended January 25, 2015 of The Fresh Market, Inc. and our report dated March 20, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
Charlotte, North Carolina
March 20, 2015

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of
The Fresh Market, Inc.

We have audited the accompanying consolidated balance sheets of The Fresh Market, Inc. as of January 25, 2015 and January 26, 2014, and the related consolidated statements of comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended January 25, 2015. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Fresh Market, Inc. at January 25, 2015 and January 26, 2014, and the consolidated results of its operations and its cash flows for each of the three years in the period ended January 25, 2015, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), The Fresh Market, Inc's. internal control over financial reporting as of January 25, 2015, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 20, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
Charlotte, North Carolina
March 20, 2015

The Fresh Market, Inc.
Consolidated Balance Sheets
(In thousands, except share amounts)

	January 25, 2015	January 26, 2014
Assets		
Current assets:		
Cash and cash equivalents	$48,486	$11,745
Accounts receivable	12,442	11,098
Inventories	61,237	55,656
Prepaid expenses and other current assets	4,633	4,304
Income tax benefit	622	1,692
Deferred income taxes	6,957	3,267
Total current assets	134,377	87,762
Property and equipment, net	392,194	373,449
Deferred income taxes	1,452	—
Other assets	9,429	8,417
Total assets	$537,452	$469,628
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$45,592	$46,942
Accrued liabilities	74,641	63,694
Total current liabilities	120,233	110,636
Long-term debt	—	24,700
Capital and financing lease obligations	33,337	26,069
Closed store reserves	10,187	193
Deferred income taxes	929	12,017
Deferred rent	13,797	13,460
Deferred lease incentives	14,117	13,347
Other liabilities	16,065	12,941
Total noncurrent liabilities	88,432	102,727
Commitments and contingencies (Notes 3, 6, and 14)		
Stockholders' equity:		
Preferred stock – $0.01 par value; 40,000,000 shares authorized, none issued	—	—
Common stock – $0.01 par value; 200,000,000 shares authorized, 48,392,201 and 48,260,804 shares issued and outstanding as of January 25, 2015 and January 26, 2014, respectively	483	483
Additional paid-in capital	122,526	113,029
Retained earnings	205,778	142,753
Total stockholders' equity	328,787	256,265
Total liabilities and stockholders' equity	$537,452	$469,628

See accompanying notes to consolidated financial statements.

The Fresh Market, Inc.
Consolidated Statements of Comprehensive Income
(In thousands, except share and per share amounts)

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Sales	$1,753,166	$1,511,657	$1,329,131
Cost of goods sold (exclusive of depreciation shown separately)	1,158,546	996,301	877,433
Gross profit	594,620	515,356	451,698
Operating expenses:			
Selling, general and administrative expenses	406,452	349,813	303,495
Impairments and store closure costs	22,589	27,505	976
Depreciation	61,966	54,657	45,741
Income from operations	103,613	83,381	101,486
Interest expense	4,375	3,783	1,498
Income before provision for income taxes	99,238	79,598	99,988
Tax provision	36,213	28,791	35,855
Net income and comprehensive income	$63,025	$50,807	$64,133
Net income per share:			
Basic and diluted	$1.30	$1.05	$1.33
Weighted average common shares outstanding:			
Basic	48,298,653	48,206,879	48,076,675
Diluted	48,475,735	48,394,338	48,294,299

See accompanying notes to consolidated financial statements.

The Fresh Market, Inc.
Consolidated Statements of Stockholders' Equity
(In thousands, except share amounts

	Common Stock, $0.01 par value				
	Common Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings	Total Stockholders' Equity
As of January 29, 2012	48,040,083	$481	$98,622	$27,813	$ 126,916
Exercise of share-based awards	77,209	1	1,717	—	1,718
Issuance of common stock pursuant to restricted stock units	16,964	—	—	—	—
Issuance of common stock pursuant to employee stock purchase plan	3,751	—	185	—	185
Vesting of restricted stock awards, non-employee directors	6,613	—	—	—	—
Withholding tax on restricted stock unit vesting	—	—	(492)	—	(492)
Share-based compensation	—	—	4,259	—	4,259
Tax benefit related to exercise of share-based awards	—	—	1,140	—	1,140
Net income	—	—	—	64,133	64,133
As of January 27, 2013	48,144,620	$482	$105,431	$91,946	$ 197,859
Exercise of share-based awards	84,453	1	2,058	—	2,059
Issuance of common stock pursuant to restricted stock units	19,203	—	—	—	—
Issuance of common stock pursuant to employee stock purchase plan	5,290	—	226	—	226
Vesting of restricted stock awards, non-employee directors	7,238	—	—	—	—
Withholding tax on restricted stock unit vesting	—	—	(494)	—	(494)

Share-based compensation	—	—	5,239	—	5,239
Tax benefit related to exercise of share-based awards	—	—	569	—	569
Net income	—	—	—	50,807	50,807
As of January 26, 2014	48,260,804	$483	$113,029	$142,753	$ 256,265
Exercise of share-based awards	88,108	—	1,938	—	1,938
Issuance of common stock pursuant to restricted stock units	22,729	—	—	—	—
Issuance of common stock pursuant to employee stock purchase plan	5,056	—	170	—	170
Vesting of restricted stock awards, non-employee directors	11,374	—	—	—	—
Vesting of executive restricted stock awards	4,130	—	—	—	—
Withholding tax on restricted stock unit vesting	—	—	(468)	—	(468)
Share-based compensation	—	—	7,533	—	7,533
Tax benefit related to exercise of share-based awards	—	—	324	—	324
Net income	—	—	—	63,025	63,025
As of January 25, 2015	48,392,201	$483	$122,526	$205,778	$ 328,787

See accompanying notes to consolidated financial statements.

The Fresh Market, Inc.
Consolidated Statements of Cash Flows
(In thousands)

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Operating activities			
Net income	$63,025	$50,807	$64,133
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	62,163	54,878	45,962
Loss on disposals of property and equipment	2,006	311	170
Impairment of property and equipment	8,961	26,828	—
Gain on assignment of capital lease	(1,508)	—	—
Share-based compensation	7,533	5,239	4,259
Excess tax benefits from share-based compensation	(324)	(569)	(1,140)
Deferred income taxes	(16,230)	(11,519)	(6,339)
Change in assets and liabilities:			
Accounts receivable	(1,344)	(4,268)	(2,280)
Inventories	(5,581)	(11,671)	(6,189)
Prepaid expenses and other assets	(1,003)	351	(6,150)
Income tax benefit	1,070	—	—
Accounts payable	(1,350)	11,308	846
Closed store reserves	9,487	(170)	
Accrued and other liabilities	16,120	18,847	15,846
Net cash provided by operating activities	143,025	140,372	109,118
Investing activities			
Purchases of property and equipment	(90,182)	(122,366)	(81,107)
Proceeds from sale of property and equipment	8,004	119	6,698
Payments for lease acquisition costs	—	—	(17,204)
Net cash used in investing activities	(82,178)	(122,247)	(91,613)
Financing activities			
Borrowings on revolving credit facility	138,233	513,621	466,324
Payments made on revolving credit facility	(162,933)	(530,921)	(488,324)
Payments made for debt issuance costs	(534)	—	—
Payments made on capital and financing lease obligations	(836)	(177)	—
Proceeds from issuance of common stock pursuant to employee stock purchase plan	170	226	185
Excess tax benefits from share-based compensation	324	569	1,140
Payments made on withholding tax for restricted stock unit vesting	(468)	(494)	(492)
Proceeds from exercise of share-based compensation awards	1,938	2,059	1,718
Net cash used in financing activities	(24,106)	(15,117)	(19,449)

Net increase (decrease) in cash and cash equivalents	36,741	3,008	(1,944)
Cash and cash equivalents at beginning of period	11,745	8,737	10,681
Cash and cash equivalents at end of period	$48,486	$11,745	$8,737
Supplemental disclosures of cash flow information:			
Cash paid during the period for interest	$4,188	$2,483	$1,000
Cash paid during the period for taxes	$51,332	$47,609	$41,128
Non-cash investing and financing activities:			
Property and equipment acquired through capital and financing lease obligations	$9,644	$40,511	$2,196

See accompanying notes to consolidated financial statements.

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The Fresh Market, Inc.

Notes to Consolidated Financial Statements
(In thousands, except share and per share data)

1. Description of Business

The Fresh Market, Inc., a Delaware corporation, and its consolidated subsidiaries (collectively “The Fresh Market” or the “Company”), is a growing specialty retailer focused on creating an extraordinary food shopping experience for its customers. Since opening its first store in 1982, the Company has offered high-quality food products, with an emphasis on fresh, premium perishables and an uncompromising commitment to customer service. The Company seeks to provide an attractive, convenient shopping environment while offering its customers a compelling combination of price and value.

2. Summary of Significant Accounting Policies

Basis of Presentation

On June 12, 2012, the Company, certain stockholders of the Company who owned shares of Company common stock prior to the initial public offering and certain officers of the Company (the “2012 Selling Stockholders”) and an underwriter entered into an Underwriting Agreement pursuant to which the 2012 Selling Stockholders offered and sold 11,538,112 shares of Company common stock at $50.50 per share in an underwritten public offering. The public offering of the 11,538,112 shares closed on June 18, 2012. The Company did not receive proceeds from the sale of these shares and expensed approximately $500 of costs associated with the offering during the year ended January 27, 2013. This amount is included in the “Selling, general and administrative expenses” line item on the Consolidated Statements of Comprehensive Income.

Definition of Fiscal Year

The Company reports its results of operations on a 52- or 53-week fiscal year ending on the last Sunday in January. The years ended January 25, 2015, January 26, 2014, and January 27, 2013 were 52-week years.

Principles of Consolidation

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"). The Company’s wholly-owned subsidiaries are consolidated and all intercompany accounts and transactions are eliminated upon consolidation.

Use of Estimates

The preparation of financial statements in conformity with U.S. 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

In certain instances, amounts previously reported in the consolidated financial statements have been reclassified to conform to current year presentation. The reclassifications have no effect on net income or stockholders' equity as previously reported.

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The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Reportable Segments

The Company has determined that it has only one reportable segment. The Company's revenues come from the sale of items at its specialty food stores. The Company's primary focus is on perishable food categories, which include meat, seafood, produce, deli, bakery, floral, sushi and prepared foods. Non-perishable categories consist of traditional grocery, frozen and dairy products as well as bulk, coffee and candy, beer and wine, and health and beauty. The following is a summary of the percentages for the sales of perishable and non-perishable items:

	Year Ended		
	January 25, 2015	January 26, 2014	January 27, 2013
Perishable	65.5%	65.4%	65.8%
Non-perishable	34.5%	34.6%	34.2%

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, cash on deposit with banks and credit and debit card sales transactions which settle within a few business days of the reporting date.

Accounts Receivable

Accounts receivable consist primarily of receivables from lessors for tenant improvement allowances, from vendors for certain promotional programs and other miscellaneous receivables and are presented net of an allowance for estimated uncollectible amounts of $159 and $186 at January 25, 2015 and January 26, 2014, respectively.

Inventories

The Company's inventories are stated at the lower of cost or market. For approximately 96% of the Company's inventories at both January 25, 2015 and January 26, 2014, cost was determined using the last-in, first-out, or LIFO method. This method results in a better matching of the Company's costs and revenues. Under the LIFO method, the cost assigned to items sold is based on the cost of the most recent items purchased. As a result, the costs of the first items purchased remain in inventory and are used to value ending inventory. The excess of the current cost of inventories over the LIFO value, or the LIFO reserve, was $7,743 and $6,727 at January 25, 2015 and January 26, 2014, respectively.

The Company determines the current cost of its inventories using the first-in, first-out, or FIFO method. The FIFO value of inventories includes cost of goods and freight, net of vendor rebates and discounts. If the FIFO method had been used for all inventories, the carrying value of inventories would have been $68,980 and $62,383 at January 25, 2015 and January 26, 2014, respectively.

Property and Equipment

Except for capital and financing lease assets, property and equipment is stated at cost. Depreciation is provided using the straight-line method over the following estimated useful lives:

Buildings	30 years
Leaseholds and land improvements	10 - 15 years
Store fixtures and equipment	3 - 10 years

Office furniture, fixtures, and equipment	5 - 10 years
Automobiles	5 years
Software	3 years

Depreciation of leasehold and land improvements is recognized over the shorter of the estimated useful life of the asset or the term of the lease. The term of the lease includes renewal options for additional periods if the exercise of the renewal is considered to be reasonably assured.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Capital and financing lease assets in the amount of $46,506 and $42,707 are incorporated with buildings, which is included in the "Property and equipment, net" line item on the accompanying Consolidated Balance Sheets as of January 25, 2015 and January 26, 2014, respectively. Accumulated depreciation related to capital and financing lease assets as of January 25, 2015 and January 26, 2014 was $3,972 and $2,029, respectively. Capital leases are recorded at the lesser of the net present value of the minimum lease payments or fair value. Financing lease assets are recorded at fair value. Depreciation on capital and financing leases is recognized over the lesser of the asset's lease term or economic life of the property.

When property and equipment is sold or retired, the cost and accumulated depreciation are removed from the accounts and the resulting gain or loss is recognized in the "Selling, general and administrative expenses" line item on the accompanying Consolidated Statements of Comprehensive Income. Expenditures for maintenance and repairs are charged to expense as incurred.

Interest costs incurred on borrowed funds during the period of construction of capital assets are capitalized as a component of the cost of those assets. Interest costs of $336, $464, and $240 were capitalized during the years ended January 25, 2015, January 26, 2014, and January 27, 2013, respectively.

Impairment of Long-Lived Assets

The Company assesses its long-lived assets, principally leasehold and land improvements, store fixtures, and equipment, for possible impairment whenever events or changes in circumstances, such as unplanned or significant negative operating cash flow or the manner in which the Company intends to utilize its long-lived assets, indicate the carrying value of an asset or asset group may not be recoverable. When assessing whether impairment exists, the Company aggregates long-lived assets at the individual store level, which the Company considers to be the lowest level for which independent identifiable cash flows are available. Impairment evaluations for individual stores take into consideration a store’s historical and projected operating cash flows, the period of time the store has been open, and the operating performance in the related market. Recoverability is evaluated by comparing the carrying amount of the asset group to the future undiscounted cash flows expected to be generated by the asset group. If the carrying value of the asset group is greater than the future undiscounted cash flows, an impairment exists and must be measured and a loss is recognized for any excess of the carrying value over the estimated fair value of the asset group. The fair value is estimated based on discounted future cash flows and/or market values of the long-lived assets.

Store Closure Costs

The Company recognizes a charge and related reserve for future operating lease payments associated with retail stores that are no longer being utilized in its current operations. The reserve is calculated using the present value of the remaining noncancelable lease payments after the cease use date less an estimate of subtenant income. If subtenant income is expected to be higher than the current lease payments, no reserve is recorded. Lease payments included in the closed store reserve are expected to be paid over the remaining terms of the respective leases, which range from approximately eight to fourteen years. The Company's assumptions about subtenant income are based on its experience and knowledge of the area in which the closed property is located, guidance received from local brokers and agents, commercial market value analysts, and existing economic conditions. As part of its analysis, the Company may acquire third-party fair value reports, which provide independent estimates of the fair values of similar rental properties. Adjustments to the closed store reserve relate primarily to changes in subtenant income and other assumptions differing from original estimates, as well as reductions to the reserve resulting from periodic lease payments. Adjustments are recorded for changes in estimates in the period in which the change becomes known.

Revenue Recognition

Revenue is recognized at the point of sale, net of coupons and discounts. Sales taxes are not included in revenue. As of January 25, 2015, the Company operated 169 stores in 27 states.

Gift Cards

A wholly owned subsidiary of the Company sells its gift cards to its customers. There are no administrative fees on unused gift cards and the gift cards do not have an expiration date. Gift card sales are recorded as a liability to unearned gift card revenue when sold and are recognized as revenue when either the gift card is redeemed or the likelihood of the gift card being redeemed is remote (“gift card breakage”). The Company's gift card breakage rate is based upon historical redemption patterns and it recognizes breakage revenue utilizing the redemption recognition method.

Gift card breakage recognized for the years ended January 25, 2015, January 26, 2014, and January 27, 2013 was not material. Any future revisions to the estimated breakage rate may result in changes in the amount of breakage revenue recognized in future periods.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Cost of Goods Sold

Cost of goods sold consists of the cost of inventory sold during the period, including the direct costs of purchased merchandise, distribution and supply chain costs, buying costs, a LIFO adjustment, supplies and store occupancy costs. Store occupancy costs include rent, common area maintenance, real estate taxes, personal property taxes, insurance, licenses and utilities related to the stores used in the Company's operations. Rebates and discounts from vendors are recorded as the related purchases are made and are recognized as a reduction to cost of goods sold as the related inventory is sold.

Selling, General and Administrative Expenses

Selling, general and administrative expenses include certain retail store and corporate costs, including compensation (both cash and share-based), pre-opening expenses, marketing and advertising and other direct store and corporate administrative costs. Pre-opening expenses are costs associated with the opening of new stores including travel, recruiting, relocating and training personnel and other miscellaneous costs. Pre-opening costs and costs incurred for producing and communicating advertising are expensed when incurred. Advertising costs totaled $5,788, $4,263, and $3,826 for the years ended January 25, 2015, January 26, 2014, and January 27, 2013, respectively.

Leases

For leases classified as operating leases, the lease agreements generally include rent holidays and rent escalation provisions and may include contingent rent provisions for percentage of sales in excess of specified levels. The Company recognizes rent holidays, including the time period during which the Company has control of the property prior to the opening of the store, as well as escalating rent provisions, as deferred rent expense and amortizes these balances on a straight-line basis over the term of the lease. For lease agreements that require the payment of contingent rents based on a percentage of sales above stipulated minimums, the Company begins accruing an estimate for contingent rent expense when it is determined that it is probable the specified levels of sales in excess of the stipulated minimums will be reached during the year. Reimbursement from a landlord for tenant improvements is classified as an incentive and included in the "Deferred lease incentives" line item on the accompanying Consolidated Balance Sheets. The deferred rent credit is amortized as a reduction to rent expense on a straight-line basis over the term of the lease.

For leases that are classified as capital leases, the capital lease asset is recorded as a building, which is included in the “Property and equipment, net” line item and a corresponding amount is recorded as a capital lease obligation in the “Capital and financing lease obligations” line item on the accompanying Consolidated Balance Sheets at an amount equal to the lesser of the net present value of minimum lease payments to be made over the lease term or the fair value of the property being leased. The Company allocates each lease payment between a reduction of the lease obligation and interest expense using the effective interest method.

With certain leases, the Company is involved with the construction of the building and the Company is considered the owner of the building for accounting purposes. The Company capitalizes the amount of total project costs incurred during the construction period as construction in progress. At the completion of the construction project, the Company evaluates whether the transfer to the landlord meets the requirements for sale-leaseback accounting treatment. A sale and leaseback of the asset is deemed to occur when construction of the asset is complete and the lease term begins and the relevant sale-leaseback accounting criteria are met. Any gain or loss from the transaction is deferred and amortized as rent expense on a straight-line basis over the term of the lease. If the lease does not meet the criteria for sale-leaseback accounting, the Company records the financing lease asset as a building, which is included in the “Property and equipment, net” line item, and a corresponding financing obligation in the “Capital and financing lease obligations” line item on its Consolidated Balance Sheets. The Company allocates each lease payment between a reduction of the lease obligation and interest expense using the effective interest method.

During the year ended January 25, 2015, the Company entered into a sale-leaseback transaction involving one of its store locations. The store is being leased from the buyer-lessor over an initial lease term of 15 years and is classified as an operating lease. The Company determined it retained the lease rights to the property and preserved the benefits and risks incident to ownership, and thus the $212 gain which resulted from the net $7,855 transaction proceeds was deferred and is being amortized as a reduction to rent expense over the 15-year initial lease term.

During the year ended January 27, 2013, the Company entered into a sale-leaseback transaction involving one of its store locations. The store is being leased from the buyer-lessor over an initial lease term of 15 years and is classified as an operating lease. The Company determined it retained the lease rights to the property and preserved the benefits and risks incident to ownership, and thus the $1,258 gain which resulted from the net $6,604 transaction proceeds was deferred and is being amortized as a reduction to rent expense over the 15-year initial lease term.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)
Share-based Compensation - 2010 Omnibus Incentive Compensation Plan
The Company grants options to purchase common stock under The Fresh Market, Inc. 2010 Omnibus Incentive Compensation Plan (“2010 Omnibus Incentive Compensation Plan”), which was adopted and approved by the Board of Directors and the Company's stockholders in 2010 and reapproved by the Company's stockholders in 2012. The 2010 Omnibus Incentive Compensation Plan provides for the grant of options intended to qualify as incentive stock options, nonqualified stock options, stock appreciation rights, restricted stock awards ("RSAs"), restricted stock units (“RSUs”), performance compensation awards, cash incentive awards, deferred share units and other equity-based and equity-related awards.
In accordance with ASC 718, Compensation-Stock Compensation, the fair value of each option award is estimated on the grant date using the Black-Scholes option-pricing model. This model requires the input of certain assumptions, including the expected life of the share-based award, stock price volatility, dividend yield and interest rate. Because there is limited history for the Company's common stock, the expected life and volatility assumptions are based on historical data from similar entities, which comprise the Company's "peer group." The Company's assessment of its peer group includes considerations such as the subject companies' plan characteristics and principal populations as well as industry, stage of life cycle, size and financial leverage. Since the Company's initial public offering, it has not declared dividends and it does not plan to pay any dividends in the future. The risk-free rate for periods in the contractual life of the option is based on the U.S. Treasury constant maturities in effect at the time of the grant.
The fair value of RSUs and RSAs is based on the closing price of the Company's common stock on the date of grant. The RSU awards are based on a four year graded vesting schedule over the requisite service period and the Company recognizes compensation expense on a straight-line basis for RSUs net of estimated forfeitures. RSAs issued to independent directors vest pursuant to the 2010 Omnibus Incentive Compensation Plan at the earlier of one year or the next annual meeting of stockholders. The Company recognizes compensation expense for RSAs on a straight-line basis net of estimated forfeitures over the vesting period.
Executive RSAs are comprised of two types: RSAs that are subject to three-year cliff-based vesting, and RSAs that vest in annual 25% increments over a four-year period beginning on the grant date. Upon vesting, the risk of forfeiture and restrictions on transferability lapse. The Company recognizes the related compensation expense on a straight-line basis, net of estimated forfeitures, over the required service period.
The Company recognizes the estimated fair value of performance-based awards as share-based compensation expense over the performance period based upon its determination of whether it is probable that the performance targets will be achieved. The Company assesses the probability of achieving the performance targets at each reporting period. Cumulative adjustments, if any, are recorded to reflect subsequent changes in the estimated outcome of performance-related conditions. The fair value of the performance-based awards is based on the fair market value of the Company's common stock on the date of grant.

Income Taxes

The Company must make certain estimates and judgments in determining income tax expense for financial statement purposes. The amount of taxes currently payable or refundable is accrued, and deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets are also recognized for realizable loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities for a change in tax rates is recognized in income in the period that includes the enactment date.

The Company applies the provisions of the authoritative guidance on accounting for uncertainty in income taxes that was issued by the Financial Accounting Standards Board ("FASB"). Pursuant to this guidance, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities based on the technical merits of the position. The tax benefits recognized in the consolidated financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The authoritative guidance also addresses other items related to uncertainty in income taxes including derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition.

The Company applies the provisions of ASC 740-10, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 ("ASC 740-10"), which prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Additionally, ASC

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)
740-10 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition.

Recent Accounting Pronouncements

In April 2014, the FASB issued Accounting Standards Update No. 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity (ASU 2014-08), to change the criteria for determining which disposals can be presented as discontinued operations and enhance the related disclosure requirements. The guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2014 with early adoption permitted for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued. Upon adoption of this standard, the Company will be required to evaluate whether a disposal meets the discontinued operations requirements under ASU 2014-08. The Company does not expect the adoption of this standard to have a material impact on its consolidated financial statements.

In May 2014, the FASB issued Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09), which amended the existing accounting standards for revenue recognition. ASU 2014-09 establishes principles for recognizing revenue upon the transfer of promised goods or services to customers, in an amount that reflects the expected consideration received in exchange for those goods or services. It is effective for annual reporting periods beginning after December 15, 2016. Early adoption is not permitted. The standards may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of initial application. The Company is currently in the process of evaluating the effect this guidance will have on its consolidated financial statements and related disclosures.

In June 2014, the FASB issued Accounting Standards Update No. 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period (ASU 2014-12). The guidance requires that a performance target that affects vesting and could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in FASB Accounting Standards Codification (ASC) 718, Compensation-Stock Compensation, as it relates to such awards. ASU 2014-12 is effective for annual reporting periods, and interim periods within those annual reporting periods, beginning after December 15, 2015 with early adoption permitted. The Company does not expect that the adoption of this guidance will have a material impact on its consolidated financial statements and related disclosures.

3. Long-Term Debt

Long-term debt is as follows:

	Year Ended	
	January 25, 2015	January 26, 2014

Unsecured revolving credit note, with maximum available borrowings of $175,000 at January 25, 2015 and January 26, 2014, interest payable monthly at one-month LIBOR plus a margin, with a total stated interest rate of 1.1% and 1.4% for the years ended January 25, 2015 and January 26, 2014, respectively	$—	$24,700

On June 12, 2014, the Company entered into an unsecured revolving credit agreement with Bank of America, N.A., as Administrative Agent, Swing Line Lender and Letter of Credit Issuer, and the several lenders party thereto (the “2014 Credit Agreement”). The 2014 Credit Agreement refinanced and replaced the Company's senior unsecured revolving credit facility under that certain Credit Agreement, dated February 22, 2011, with Bank of America, N.A., as Administrative Agent, Swing Line Lender and Letter of Credit Issuer, and the several lenders party thereto (the “2011 Credit Agreement”). The 2011 Credit Agreement was terminated effective June 12, 2014 upon the Company entering into the 2014 Credit Agreement.

The 2014 Credit Agreement matures June 12, 2019 and is available to provide support for working capital, capital expenditures and other general corporate purposes, including permitted acquisitions and issuance of letters of credit. While the Company currently has no material domestic subsidiaries, other entities will guarantee its obligations under the 2014 Credit Agreement if and when they become material domestic subsidiaries of the Company during the term of the 2014 Credit Agreement.

The Fresh Market, Inc.

Notes to Consolidated Financial Statements - (continued)

3. Long-Term Debt (continued)

The 2014 Credit Agreement provides for total borrowings of up to $175,000. Under the terms of the 2014 Credit Agreement, the Company is entitled to request an increase in the size of the facility by an amount not exceeding $100,000 in the aggregate. If the existing lenders elect not to provide the full amount of a requested increase, or in lieu of accepting offers from existing lenders to increase their commitments, the Company may designate one or more other lenders to become a party to the 2014 Credit Agreement, subject to the approval of the Administrative Agent. The 2014 Credit Agreement includes a letter of credit sublimit of $60,000, of which $25,434 was outstanding at January 25, 2015, and the 2011 Credit Agreement included a letter of credit sublimit of $25,000, of which $13,667 was outstanding at January 26, 2014. The beneficiaries of these letters of credit are primarily the Company’s workers’ compensation and general liability insurance carriers. The 2014 Credit Agreement also includes a swing line sublimit of $15,000.

At the Company’s option, revolving loans under the 2014 Credit Agreement bear interest at (i) the London Interbank Offered Rate ("LIBOR") plus an applicable margin that ranges from 0.90% to 2.00%, (ii) the Eurodollar rate plus an applicable margin that ranges from 0.90% to 2.00%, or (iii) the base rate plus an applicable margin that ranges from 0% to 1.00%, where the base rate is defined as the greatest of: (a) the federal funds rate plus 0.50%, (b) Bank of America’s prime rate, and (c) the Eurodollar rate plus 1.00%. As of January 25, 2015, there were no outstanding borrowings under the 2014 Credit Agreement; as of January 26, 2014, all outstanding borrowings under the 2011 Credit Agreement bore interest at LIBOR plus an applicable margin.

The commitment fee calculated on the unused portions of the 2014 Credit Agreement ranges from 0.125% to 0.250% per annum.

The 2014 Credit Agreement contains a number of affirmative and restrictive covenants, including limitations on the Company's ability to grant liens, incur additional debt, pay dividends, redeem its common stock, make certain investments and engage in certain merger, consolidation or asset sale transactions.

4. Fair Value Measurements

ASC 820, Fair Value Measurements, requires fair value measurements be classified and disclosed in one of the following pricing categories:

- Level 1 - Quoted prices in active markets for identical assets or liabilities as of the reporting date.
- Level 2 - Observable inputs other than quoted prices in active markets included for identical assets and liabilities.
- Level 3 - Unobservable inputs in which there is little or no market data available, which require the reporting entity to develop its own assumptions.

The carrying amounts of cash and cash equivalents, accounts receivable, restricted cash, accounts payable, accrued liabilities and other accrued expenses approximate fair value because of their short maturity. The carrying amount of long-term debt

approximates fair value because the advances under this instrument bear variable interest rates which reflect market changes to interest rates and contain variable risk premiums based on certain financial ratios achieved by the Company. The fair value estimate of our long-term debt is a Level 2 measurement.
The section below, Non-Recurring Fair Value Measurements, presents long-lived assets that were measured and recorded at fair value on a nonrecurring basis and the total impairment charges recorded during the years ended January 25, 2015 and January 26, 2014.

Non-Recurring Fair Value Measurements
During the years ended January 25, 2015 and January 26, 2014, the Company recorded impairment charges of $8,961 and $26,828 for certain real estate and other store related assets, writing down the assets to their estimated fair value of $10,872 and $21,682, respectively. For the years ended January 25, 2015 and January 26, 2014, the Company performed an impairment analysis of its long-lived assets and determined that the assets referred to above were impaired since the estimated undiscounted cash flows associated with the respective assets were less than the carrying value. These charges were based, in part, on estimates that used Level 3 inputs within the fair value hierarchy. The fair value of real estate was primarily based on a market approach and the fair value for non-real estate assets, such as leasehold improvements and fixtures, was based on a cost approach, both of which included assistance from analysis by third party specialists. The market approach is a valuation method which estimates fair value based on market transactions and sales of comparable assets. Inputs used in the market approach

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

4. Fair Value Measurements (continued)
include comparable sales transaction data, market rents and capitalization rates for the related assets. The cost approach is a valuation method which estimates the price that would be received to sell the store related assets in an orderly transaction between market participants at the measurement date. Inputs used in the cost approach primarily include current costs trend factors, which are meant to adjust the historical price of an asset to a current price by capturing all inflationary forces on the subject asset, and functional and economic obsolescence factors, which are based on the expected life and expected use of the asset. Additionally, the assessment of the fair value for certain real estate assets during the year ended January 26, 2014, utilized a discounted cash flow approach. The primary inputs for the discounted cash flow approach include projected cash flows expected to be generated by the assets and a discount rate.
The following tables show the fair value of the Company's long-lived assets that have been adjusted to fair value on a non-recurring basis which had a significant impact on the Company's results of operations for the years ended January 25, 2015 and January 26, 2014.

Description	Carrying Value Prior to Impairment	Fair Value Measurement as of January 25, 2015			Impairment Charge Recognized
		Level 1	Level 2	Level 3	
	(in thousands)				
Long-lived assets held and used	$19,833	$—	$—	$10,872	$8,961

Description	Carrying Value Prior to Impairment	Fair Value Measurement as of January 26, 2014			Impairment Charge Recognized
		Level 1	Level 2	Level 3	
	(in thousands)				
Long-lived assets held and used	$48,510	$—	$—	$21,682	$26,828

5. Impairments and Store Closure Costs
Impairments
During the years ended January 25, 2015 and January 26, 2014, the Company concluded the long-lived assets related to certain stores were impaired. As a result, impairment charges of $8,961 and $26,828 were recognized to write down the carrying value of the assets to fair value for the years ended January 25, 2015 and January 26, 2014, respectively. Refer to Note 4 for a discussion of the methods and inputs used to estimate the fair value of those asset groups.
Store Closure Costs

Store closure and exit costs for the years ended January 25, 2015, January 26, 2014, and January 27, 2013, were $13,628, $677, and $976, respectively. Included in those amounts are lease obligation costs related to closed stores, which represent the present value of the remaining non-cancelable lease payments required under operating leases for the closed stores, less an estimate of subtenant income, employee severance costs, loss on disposal of assets, other costs associated with exiting the stores, and other costs. During the year ended January 25, 2015, the Company closed four stores and recorded a gain on the assignment of a capital lease for one of the stores closed during the year.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

5. Impairments and Store Closure Costs (continued)

Store closure and exit costs for the years ended January 25, 2015, January 26, 2014 and January 27, 2013 were as follows:

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Lease obligation costs	$11,223	$653	$954
Gain on assignment of capital lease	(1,508)	—	—
Employee and severance costs	768	—	—
Loss on disposals of assets	1,896	—	—
Other costs	1,249	24	22
Total store closure and exit costs	$13,628	$677	$976

Closed Store Reserves

Activity for the closed store reserve during the years ended January 25, 2015, January 26, 2014, and January 27, 2013 was as follows:

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Beginning balance	$1,812	$1,982	$1,969
Additions and adjustments	14,498	656	936
Payments	(5,011)	(826)	(923)
Ending balance	$11,299	$1,812	$1,982

6. Leases

The Company leases the majority of its retail store locations, its administrative offices, and certain equipment, under noncancelable operating lease agreements that expire from 2015 to 2032. The store location leases generally have an initial term ranging from 10 to 15 years and contain renewal options ranging from 15 to 30 years with increased rental rates during the option periods.

The Company leases certain retail store locations under capital and financing lease agreements that expire from 2024 to 2035. The store locations have initial lease terms that range from 10 to 15 years and contain renewal options ranging from 15 to 25 years.

The Company does not receive a material amount of sublease rents from subtenants in its leased properties.

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The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

6. Leases (continued)

Future minimum lease commitments for the Company's capital and financing lease obligations and operating lease commitments having initial or remaining terms in excess of one year are as follows:

	Capital and Financing Lease Obligations	Operating Leases
2015	$5,038	$56,450
2016	5,216	58,995
2017	5,216	58,718
2018	5,216	55,346
2019	5,252	55,616
Thereafter	44,208	240,050
Total lease commitment	70,146	$525,175
Non-cash gain on future disposition of property	838	
Less amount representing interest, 10.8% weighted average interest rate	(36,404)	
Present value of obligations under capital and financing lease obligations	34,580	
Less current portion	(1,243)	
Noncurrent capital and financing lease obligations	$33,337	

Total rent expense, net of subtenant lease income, for the years ended January 25, 2015, January 26, 2014, and January 27, 2013 was as follows:

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Minimum rentals	$48,603	$43,047	$36,880
Contingent rentals	519	434	505
	$49,122	$43,481	$37,385

The Company also incurs other lease-related expenses such as real estate taxes, insurance and maintenance that are generally based on the Company's pro-rata share of the total square footage of the property being leased. Except for capital and financing leases, the Company's store lease expenses are recorded in the "Cost of goods sold" line item on the accompanying Consolidated Statements of Comprehensive Income. Lease expenses related to the Company's corporate offices are recorded in the "Selling, general and administrative expenses" line item on the Consolidated Statements of Comprehensive Income. Additionally, lease expenses related to closed stores are recorded in the "Impairments and store closure costs" line item on the Consolidated Statements of Comprehensive Income.

In November 2012, as part of an agreement with an entity and various related parties of the entity, the Company acquired certain lease rights to four new store locations.

The agreement required an inducement payment of approximately $17,200, which was allocated equally among the four store locations. Approximately $3,000 of the $17,200 payment was paid to the entity upon execution of the agreement and was recorded in the "Other assets" line item on the Consolidated Balance Sheets as of January 27, 2013. The remainder of the payment was placed in escrow, and was paid out as each of the properties was delivered to the Company in the condition specified by agreement. The sum of the payments was applied equally to reduce the related capital lease obligation upon transfer of the property during the year ended January 26, 2014. The $17,200 payment paid to the entity and into the escrow account was previously classified as a cash outflow from operating activities during the year ended January 27, 2013. However, as a result of the change in the classification of the related leases from operating to capital, the payment is classified as cash used in investing activities during the year ended January 27, 2013 on the accompanying Consolidated Statements of Cash Flows.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

7. Employee Benefits

Accrued Compensated Absences

The Company provides its employees with paid annual leave that may be used for any purpose and varies in duration based on years of service to the Company. Per the Company's policy, except where applicable state law requires otherwise, paid annual leave is fully earned and awarded on January 1 of each year (or, if later, the employee's first day worked during such year) to eligible employees of the Company on December 31 of the preceding year. The amount of paid annual leave awarded is based on an employee's number of years of service at December 31 of the preceding year. The Company's policy does not provide for a carryforward of unused balances to future years, except where required by law. The Company accrues the value of the annual leave to be awarded on January 1 of the following year, less an estimate for forfeitures, ratably over the year. The Company had $7,312 and $6,307 accrued for paid annual leave as of January 25, 2015 and January 26, 2014, respectively.

Deferred Compensation Plan

The Company has a deferred compensation plan for eligible employees. Under the terms of the plan, eligible employees may defer up to 80% of their base salary and 100% of their annual bonus on a pre-tax basis. The Company will make matching contributions to the eligible employees' accounts, up to defined maximums, to compensate for matching contributions that would have been made to the eligible employees' 401(k) plan accounts had the eligible employees not participated in the deferred compensation plan. The deferred compensation plan also permits the Company to make discretionary contributions to eligible employees' accounts. Deferred amounts will be distributed in a lump sum in the event of death, termination of employment before age 55 and five years of employment, or termination of employment within two years following a change in control. In the event of termination of employment after age 55 and five years of employment, the eligible employees may elect distributions in a lump sum or by installment payments. Participants may also elect to defer amounts to in-service distribution accounts for distribution at specified dates. Distributions may also be made in the event of unforeseeable emergency.

The liability related to the deferred compensation plan was $4,289 and $3,439 as of January 25, 2015 and January 26, 2014, respectively. The Company recognized compensation expense related to the plan of $55, $45, and $63 for the years ended January 25, 2015, January 26, 2014, and January 27, 2013, respectively.

Employee Savings and Profit Sharing Plan

The Company sponsors an employee savings and profit sharing plan which is a defined contribution retirement plan subject to Section 401(k) of the Internal Revenue Code. The plan is voluntary and is available to all eligible full-time employees after 60 days of service. Prior to January 1, 2014, the plan was available to all eligible full-time employees after one year of service. The Company may, in its discretion, provide a matching contribution up to defined maximums. The expense recorded for the Company's match to the 401(k) plan was $1,200, $1,022, and $920 for the years ended January 25, 2015, January 26, 2014, and January 27, 2013, respectively.

Long-Term Cash Incentive Program

In March 2012, the Company adopted The Fresh Market, Inc. Long-Term Cash Incentive Program for Select Employees (the "Program"), in which the Company’s executive officers do not participate. The purpose of the Program is to provide incentives and reward employees for achieving specified performance goals over a given performance period. There was an incentive provided under the Program during each of the years ended January 25, 2015, January 26, 2014 and January 27, 2013. The Program awards cash bonuses to participants based upon the Company’s achievement of specified performance goals encompassing a three-year fiscal performance period. At each reporting period, the Company assesses the probability of achieving the performance goals required for payment of the target amounts for the performance period. These awards are expensed over the respective vesting period on a straight-line basis. Cumulative adjustments, if any, are recorded quarterly to reflect subsequent changes in the estimated outcome of performance-related conditions. Each participant receives a percentage of the applicable target amount for the performance period based on achievement of the performance goals and formulas. The Program’s award payouts will vary based on the achievement of the performance goals and can range from 33% to 150% for awards granted in fiscal 2012 and 2013 and 33% to 170% for awards granted in fiscal 2014. Each participant is entitled to a minimum of one-third of the total grant amount, which is paid in three annual payments over the three-year vesting period. At the end of the three-year period, the participant is eligible for a final payout, based upon the Company’s specific measurement criteria, if the threshold for the applicable performance goal is reached and the participant is employed by the Company at the end of the performance period. For the years ended January 25, 2015, January 26, 2014, and January 27, 2013, the Company recorded expense for the Program of $782, $57 and $443, respectively. The expense for the year ended January 26, 2014 includes an adjustment that reflected a decrease in the estimated cumulative payout amount based on the probability of achieving the performance criteria.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

8. Income Taxes

The income tax provision consisted of the following:

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Current:			
Federal	$45,263	$32,852	$36,056
State	7,180	7,458	6,138
Total current	52,443	40,310	42,194
Deferred:			
Federal	(15,314)	(10,175)	(5,664)
State	(916)	(1,344)	(675)
Total deferred	(16,230)	(11,519)	(6,339)
Total income tax provision	$36,213	$28,791	$35,855

A reconciliation of the statutory federal income tax rate of 35% and the Company's effective tax rate is as follows:

	Year Ended January 25, 2015	January 26, 2014	January 27, 2013
Statutory federal rate	35.00 %	35.00 %	35.00 %
State income taxes	3.78 %	4.36 %	3.44 %
Enhanced charitable food contribution	(2.12)%	(2.64)%	(2.67)%
Other	(0.17)%	(0.55)%	0.09 %
Effective tax rate	36.49 %	36.17 %	35.86 %

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

8. Income Taxes (continued)

The major components of the Company's deferred tax assets and liabilities at January 25, 2015 and January 26, 2014 are as follows:

	Year Ended January 25, 2015	January 26, 2014
Deferred Tax Assets:		
Accrued compensation	$4,395	$3,016
Accrued expenses	17,869	12,102
Deferred and share-based compensation	6,598	4,369
Excess charitable contributions	10,745	10,120
Capital and financing lease obligations	17,732	15,366
Other	61	95
Total deferred tax assets	57,400	45,068
Deferred Tax Liabilities:		
Depreciation	(47,088)	(51,023)
Inventories	(2,076)	(1,836)
Prepaid expenses	(756)	(959)
Total deferred tax liabilities	(49,920)	(53,818)
Net deferred tax asset (liability)	$7,480	$(8,750)

Deferred taxes have been classified on the Consolidated Balance Sheets as follows:

	Year Ended January 25, 2015	January 26, 2014
Current assets	$6,957	$3,267
Non-current assets	1,452	—
Non-current liabilities	(929)	(12,017)
Net deferred tax asset (liability)	$7,480	$(8,750)

The Company had a state operating loss carryforward of $353 for the year ended January 26, 2014, which was fully utilized during the year ended January 25, 2015 to offset taxable income. The state operating loss carryforward was set to expire in fiscal 2026. The Company has charitable contribution carryforwards, which are subject to a 5-year carryforward limitation, which will begin to expire during the year ending January 29, 2017.

As of January 25, 2015 and January 26, 2014, the Company had no accrued interest or penalties related to uncertain tax positions. There were no unrecognized tax benefits that would affect the Company's effective tax rate if recognized. The Company does not expect its unrecognized tax benefits to change significantly in the next 12 months. The Company's policy for recording interest and penalties associated with uncertain tax positions is to record such items as a component of income taxes. The Company files income tax returns in the U.S. Federal jurisdiction and in various state jurisdictions. The statute of limitation remains open for U.S. and certain state income tax examinations for tax years 2011 through 2014.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

9. Share-based Compensation

The Company grants share-based awards under the 2010 Omnibus Incentive Compensation Plan. At January 25, 2015, January 26, 2014, and January 27, 2013, approximately 1,900,000, 2,200,000, and 2,500,000 shares of the Company's common stock, respectively, were available for share-based awards.

Stock Options - 2010 Omnibus Incentive Compensation Plan

Options are granted at an option price equal to the closing price of the Company's common stock on the grant date and vest in 25% annual increments on each of the first four anniversaries of the grant date. Options expire ten years from the grant date. The Company uses the Black-Scholes option pricing model to estimate the fair value of stock options at the grant date.
The following table summarizes option activity under the 2010 Omnibus Incentive Compensation Plan (in thousands, except per share amounts and contractual lives in years):

	Number of Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding options at January 29, 2012	702	$25.46		
Granted	200	47.33		
Exercised	(77)	22.25		
Expired	—	—		
Forfeited	(65)	33.27		
Outstanding options at January 27, 2013	760	$30.87		
Granted	141	43.10		
Exercised	(85)	24.38		
Expired	(2)	41.41		
Forfeited	(50)	32.05		
Outstanding options at January 26, 2014	764	$33.74		
Granted	246	32.71		
Exercised	(88)	22.00		
Expired	(1)	42.93		
Forfeited	(33)	35.28		
Outstanding options at January 25, 2015	888	$34.55	7.4	$5,831
Vested/expected to vest at January 25, 2015	884	$34.54	8.4	$5,810
	523	$32.19	6.6	$4,645

Exercisable options at
January 25, 2015

Share-based compensation expense related to stock options recognized under the 2010 Omnibus Incentive Compensation Plan during the years ended January 25, 2015, January 26, 2014, and January 27, 2013, totaled $3,329, $2,917, and $2,783, respectively, and is recorded in the “Selling, general and administrative expenses” line item on the accompanying Consolidated Statements of Comprehensive Income.

The weighted average grant date fair value of options granted for the years ended January 25, 2015, January 26, 2014, and January 27, 2013 was $10.49, $16.23 and $18.58, respectively. The aggregate intrinsic value of stock options exercised was $1,523 and $1,870 for the years ended January 25, 2015 and January 26, 2014, respectively. The total fair value of shares vested was $4,645 and $3,423 for the years ended January 25, 2015 and January 26, 2014, respectively. As of January 25, 2015, January 26, 2014, and January 27, 2013, there were approximately 888,000, 764,000, and 760,000 shares of nonvested stock options outstanding and $3,214, $4,866, and $5,917 of unrecognized share-based compensation expense. The Company anticipates this expense to be recognized over a weighted average period of 2.4 years.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

9. Share-based Compensation (continued)

The fair value of the stock option grants have been estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions.

	2014		2013		2012	
Risk-free interest rate	1.63	%	0.82	%	1.20	%
Expected life, in years	4.83		5.00		5.00	
Expected volatility	34.18	%	42.29	%	43.57	%
Dividend yield	—	%	—	%	—	%
Weighted average exercise price	$32.71		$43.10		$47.33	

The risk-free interest rate is based on the U.S. Treasury constant maturities on the date of the grant for the time period equal to the expected term of the options granted. Expected volatility was calculated on the basis of the average volatilities of similar entities and considered characteristics such as industry, stage of life cycle, size, financial leverage and comparable programs and participant pools. The Company determined the use of historical volatility for similar entities represents a more accurate calculation of option fair value. Expected life is calculated in a like manner and is based upon the industry, stage of life cycle, size, financial leverage and comparable programs and participant pools. The assumptions used to calculate the fair value of options granted are evaluated and revised for new awards, as necessary, to reflect market conditions and experience.

The Company recognizes compensation expense on a straight line basis over the vesting period for all share-based awards net of estimated forfeitures.

Restricted Stock Units - 2010 Omnibus Incentive Compensation Plan

The RSUs vest in 25% annual increments on each of the first four anniversaries of the grant date and the fair value is equal to the closing price of the Company’s common stock on the grant date.

The Company recorded $1,640, $1,129, and $821 of share-based compensation expense related to these awards for the years ended January 25, 2015, January 26, 2014, and January 27, 2013, respectively, which is recorded in the "Selling, general and administrative expenses" line item on the accompanying Consolidated Statements of Comprehensive Income.

The following activity has occurred under the Company's existing restricted stock unit plan:

	Shares (in thousands)		Weighted Average Grant Date Fair Value
Balance at January 29, 2012	82		$22.00
Granted	23		48.67
Vested	(25	)	22.00
Forfeited	(7	)	25.03
Balance at January 27, 2013	73		$30.10

Granted	30	43.32
Vested	(30)	26.98
Forfeited	(3)	25.47
Balance at January 26, 2014	70	$37.26
Granted	76	33.04
Vested	(40)	31.30
Forfeited	(9)	35.52
Outstanding awards at January 25, 2015	97	$36.90
Expected to vest at January 25, 2015	95	$36.94

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The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

9. Share-based Compensation (continued)
As of January 25, 2015 and January 26, 2014, total remaining unearned compensation cost related to nonvested RSUs was approximately $2,410 and $1,835, respectively, which will be amortized over the weighted-average remaining service period of approximately 2.8 years.

Restricted Stock Awards for Non-Employee Directors - 2010 Omnibus Incentive Compensation Plan

The Company grants RSAs to its non-employee directors. RSAs vest at the earlier of one year from the date of grant or the next annual meeting of stockholders. The fair value of the RSAs is equal to the closing price of the Company’s common stock on the grant date.
The Company recorded $481, $438, and $383 of share-based compensation expense related to outstanding RSAs for non-employee directors for the years ended January 25, 2015, January 26, 2014, and January 27, 2013, respectively. Share-based compensation expense is recorded in the "Selling, general and administrative expenses” line item on the accompanying Consolidated Statements of Comprehensive Income.
The following activity has occurred under the Company's existing restricted stock award plan for non-employee directors:

	Shares (in thousands)	Weighted Average Grant Date Fair Value
Balance at January 29, 2012	6	$32.79
Granted	7	57.70
Vested	(6)	33.25
Forfeited	—	—
Balance at January 27, 2013	7	$58.00
Granted	10	49.07
Vested	(7)	58.00
Forfeited	—	—
Balance at January 26, 2014	10	$49.07
Granted	14	33.43
Vested	(13)	48.22
Forfeited	—	—
Outstanding awards at January 25, 2015	11	$32.95
Expected to vest at January 25, 2015	11	$32.95

As of January 25, 2015 and January 26, 2014, total remaining unearned compensation cost related to nonvested RSAs was $127 and $148, respectively, which will be amortized over the weighted-average remaining service period of approximately 0.4 years.

Executive Restricted Stock Awards - 2010 Omnibus Incentive Compensation Plan
The Company grants RSAs to its executive officers, which are comprised of two types of RSAs under the 2010 Omnibus Incentive Compensation Plan: RSAs that are subject to three-year cliff-based vesting, and RSAs that vest in annual 25% increments over a four-year period beginning on the grant date.
The Company recorded share-based compensation expense related to the executive RSAs of approximately $1,715 and $977 for the years ended January 25, 2015 and January 26, 2014, respectively, which is recorded in the "Selling, general and administrative expenses" line item on the accompanying Consolidated Statements of Comprehensive Income.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

9. Share-based Compensation (continued)

The following activity has occurred under the Company's existing executive restricted stock award plan:

	Shares (in thousands)	Weighted Average Grant Date Fair Value
Balance at January 27, 2013	—	$—
Granted	92	43.42
Vested	—	—
Forfeited	—	—
Balance at January 26, 2014	92	$43.42
Granted	—	—
Vested	(34)	40.56
Forfeited	(2)	42.65
Outstanding awards at January 25, 2015	56	$43.86
Expected to vest at January 25, 2015	55	$43.53

As of January 25, 2015 and January 26, 2014, total remaining unearned compensation cost related to nonvested RSAs was $1,115 and $2,896, respectively, which will be amortized over the weighted-average remaining service period of approximately 1.4 years.

Performance Share Awards - 2010 Omnibus Incentive Compensation Plan

The Performance Share Award Agreement, approved by the Board of Directors in March 2012, provides for the issuance of performance shares ("Performance Shares") under the 2010 Omnibus Incentive Compensation Plan to executive officers and certain other members of the Company's management team based upon an established performance goal.

The following activity has occurred under the Company's existing performance share awards plan:

	Shares (in thousands)	Weighted Average Grant Date Fair Value
Balance at January 29, 2012	—	$—
Granted	38	47.29
Vested	—	—
Forfeited	(4)	47.17
Balance at January 27, 2013	34	$47.31
Granted	—	—
Vested	—	—
Forfeited	(4)	47.17
Balance at January 26, 2014	30	$47.32

Granted	—	—
Vested	—	—
Forfeited	(9)	47.17
Outstanding awards at January 25, 2015	21	$47.39

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Notes to the Consolidated Financial Statements (continued)

9. Share-based Compensation (continued)

The Company did not grant any Performance Shares during the years ended January 25, 2015 or January 26, 2014. Based on the expected level of achievement of the performance condition, the Company did not recognize share-based compensation expense for the year ended January 25, 2015, and it recognized a reduction to share-based compensation expense of approximately $272 for the year ended January 26, 2014 and an expense of approximately $272 for the year ended January 27, 2013. Share-based compensation expense is recorded in the "Selling, general and administrative expenses” line item on the accompanying Consolidated Statements of Comprehensive Income.

Performance Share Units - 2010 Omnibus Incentive Compensation Plan

In March 2013, the Company adopted a Performance Share Unit Award Agreement under the 2010 Omnibus Incentive Compensation Plan. During the year ended January 25, 2015, the Company awarded approximately 46,000 performance share units ("PSUs") to its executive officers and certain other members of the Company's management team based upon an established performance goal. The PSUs are subject to performance conditions and time-based cliff vesting on the last day of the performance period, as defined below, and settle in shares of the Company's common stock upon vesting. The fair value of the PSUs is equal to the closing price of the Company’s common stock on the grant date.

The performance goal is a specified cumulative three-year earnings per share amount for the fiscal 2013 through 2015 performance period. The actual number of PSUs which vest for each participant is set at a minimum threshold of 0% of the participant's target number of PSUs and could increase to up to 170% of the target based upon performance results. Actual performance against the performance goal will be measured at the end of the performance period and approved by the Compensation Committee. Expense is recorded over the required performance period, subject to management's assessment of the expected performance outcome.

The following activity has occurred under the Company's existing performance share units plan:

	Shares (in thousands)	Weighted Average Grant Date Fair Value
Balance at January 27, 2013	—	$—
Granted	30	43.12
Vested	—	—
Forfeited	—	—
Balance at January 26, 2014	30	$43.12
Granted	46	32.57
Vested	—	—
Forfeited	(18)	37.00
Outstanding awards at January 25, 2015	58	$36.71

Based on the expected level of achievement of the performance condition, the Company recognized share-based compensation expense of $339 for the year ended January 25, 2015 and did not recognize share-based compensation expense related to the PSUs for the year ended January 26, 2014.

10. Earnings per Share

The computation of basic earnings per share is based on the number of weighted-average common shares outstanding during the period. The computation of diluted earnings per share includes the dilutive effect of common stock equivalents consisting of incremental common shares deemed outstanding from the assumed exercise of stock options, RSUs and RSAs. The Company excluded the dilutive effect of its performance shares since the related performance conditions had not been satisfied for the year ended January 25, 2015.

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Notes to the Consolidated Financial Statements (continued)

10. Earnings per Share (continued)

A reconciliation of the numerators and denominators of the basic and diluted earnings per share calculations follows (in thousands, except share and per share amounts):

	Year Ended		
	January 25, 2015	January 26, 2014	January 27, 2013
Net income available to common stockholders (numerator for basic and diluted earnings per share)	$63,025	$50,807	$64,133
Weighted average common shares outstanding (denominator for basic earnings per share)	48,299	48,207	48,077
Potential common shares outstanding:			
Incremental shares from share-based awards	177	187	217
Weighted average common shares outstanding and potential additional common shares outstanding (denominator for diluted earnings per share)	48,476	48,394	48,294
Basic and diluted earnings per share	$1.30	$1.05	$1.33

For the years ended January 25, 2015, January 26, 2014, and January 27, 2013 there were approximately 615,000, 340,000, and 251,000 shares, respectively, excluded from the computation of diluted weighted average common shares outstanding because such shares are considered anti-dilutive.

11. Insurance Reserves

The Company has insurance policies for general liability, medical and workers' compensation benefits that contain significant deductibles. The cost of these insurance claims up to the deductibles is accrued based on actual claims reported plus loss development factors. These estimates are based on historical information along with certain assumptions about future events, and are subject to change as additional information becomes available. The Company had $21,802 and $17,356 accrued related to these claims at January 25, 2015 and January 26, 2014, respectively. Insurance reserves is recorded to the "Accrued liabilities" and "Other liabilities" line items on the accompanying Consolidated Balance Sheets.

12. Supplementary Balance Sheet Information

The following reflects supplementary balance sheet information for the Company's property and equipment, net at January 25, 2015 and January 26, 2014:

	January 25, 2015	January 26, 2014
Land	$—	$2,846

Buildings	65,658	61,338
Store fixtures and equipment	364,711	323,454
Leasehold improvements	242,966	218,359
Office furniture, fixtures and equipment	13,692	14,097
Automobiles	1,315	1,370
Construction in progress	31,341	32,654
Total property and equipment	719,683	654,118
Accumulated depreciation	(327,489)	(280,669)
Total property and equipment, net	$392,194	$373,449

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Notes to the Consolidated Financial Statements (continued)

12. Supplementary Balance Sheet Information (continued)
The following reflects supplementary balance sheet information for the Company's accrued liabilities at January 25, 2015 and January 26, 2014:

	January 25, 2015	January 26, 2014
Accrued compensation and benefits	$31,698	$24,547
Accrued occupancy costs	8,569	8,716
Other accrued taxes	4,619	4,193
Accrued construction and maintenance costs	11,030	9,939
Other accrued liabilities	18,725	16,299
Total accrued liabilities	$74,641	$63,694

13. Related-Party Transactions

Tax Indemnification Agreement
In connection with the initial public offering, the Company entered into a tax indemnification agreement with the Company's stockholders prior to the offering. Pursuant to this agreement, the Company agreed that upon filing any tax return (amended or otherwise), or in the event of any restatement of the Company's taxable income, in each case for any period during which the Company was an S-corporation, it will make a payment to each stockholder on a pro rata basis in an amount sufficient so that the stockholder with the highest incremental estimated tax liability (calculated as if the stockholder would be taxable on its allocable share of the Company's taxable income at the highest applicable federal, state and local tax rates and taking into account all amounts the Company previously distributed in respect of taxes for the relevant period) receives a payment equal to its incremental tax liability. The Company also agreed to indemnify the stockholders for any interest, penalties, losses, costs or expenses (including reasonable attorneys' fees) arising out of any claim under the agreement.
Real Estate Leases
During the year ended January 26, 2014, an entity affiliated with a former officer and director of the Company, who is a family member of a member of the Company's Board of Directors as of January 25, 2015, acquired a shopping center in which the Company leases a retail store location. Lease expense related to the store since the date of such acquisition was $284 and $132 for the years ended January 25, 2015 and January 26, 2014, respectively.

14. Commitments and Contingencies

Litigation

From time to time, the Company is involved in various legal proceedings in the normal course of business, including labor and employment, premises, personal injury, product liability and general liability claims, and claims related to commercial and leasing matters. In the opinion of management, the resolution of currently pending matters, other than those described or referred to in the following paragraphs, will not have a material adverse effect on the Company's financial condition or results of operations. However, because of the nature and inherent uncertainties of litigation, the Company cannot predict with certainty the ultimate resolution of these actions and, should the outcome of these actions be unfavorable, the Company's business, financial position, results of operations or cash flows could be materially and adversely affected.

The Company reviews the status of its legal proceedings and records a provision for a liability when it is considered probable that both a liability has been incurred and the amount of the loss can be reasonably estimated. This review is updated periodically as additional information becomes available. If either or both of the criteria are not met, the Company reassesses whether there is at least a reasonable possibility that a loss, or additional losses, may be incurred. If there is a reasonable possibility that a loss may be incurred, the Company discloses the estimate of the amount of the loss or range of losses, that the amount is not material, or that an estimate of loss cannot be made. The Company expenses its legal fees as incurred.

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Notes to the Consolidated Financial Statements (continued)

14. Commitments and Contingencies (continued)
In assessing potential loss contingencies, the Company considers a number of factors, including those listed in the FASB's Accounting Standards Codification 450-20, Contingencies - Loss Contingencies, regarding assessing the probability of a loss and assessing whether a loss is reasonably estimable. Litigation can be expensive and disruptive to normal business operations. Moreover, the results of litigation are difficult to predict and the Company’s view of these matters may change as the litigation and events unfold over time. An unfavorable outcome in any legal matter, if material, could have a material adverse effect on the Company’s results of operations in the period in which the unfavorable outcome occurs and potentially in future periods.
The Company had been named in two lawsuits filed against it and other parties in South Carolina arising out of an incident in May 2011, in which certain outdoor candle products that were allegedly sold at certain of the Company's stores are alleged to have caused personal injury. During the year ended January 25, 2015, the Company and the plaintiffs in the two lawsuits resolved all claims among such parties arising out of or related to the incident. Accordingly, the claims against the Company in the two lawsuits were dismissed during the year ended January 25, 2015.
The Company is party to a lawsuit that was filed against it in U.S. District Court in Connecticut alleging that the manner in which the Company implemented and applied the fluctuating workweek method for calculating overtime due to the Company's department managers violated the federal Fair Labor Standards Act. The complaint purports to state a collective action on behalf of a class of department managers in stores in states in which the Company used the fluctuating workweek method of compensation. The Company believes that the plaintiff's claims are without merit and intends to vigorously defend itself in this proceeding. At this time, the Company cannot predict whether the Court will certify a collective action, how it will rule on the merits of the claim, and/or the scope of the potential loss in the event of an adverse outcome. Should the Company ultimately be found liable in this matter, its liability could have a material adverse effect on its results of operations for the period or periods in which it is incurred.

15. Select Quarterly Financial Data (unaudited)

The following is a summary of unaudited financial data regarding the Company's quarterly results of operations. Quarter to quarter comparisons of results of operations have been and may be materially impacted by the timing of new store openings. The Company believes that the following information reflects all normal recurring adjustments necessary for a fair presentation of the information for the periods presented. The operating results for any quarter are not necessarily indicative of results for any future period.

	Year Ended January 25, 2015			
	First Quarter (1)	Second Quarter (2)	Third Quarter (3)	Fourth Quarter (4)
Sales	$431,002	$422,227	$419,450	$480,487

Gross profit	$148,166	$143,715	$138,075	$164,664
Income from operations	$27,577	$19,126	$24,328	$32,582
Net income	$16,571	$11,390	$14,884	$20,180
Net income per share:				
Basic and diluted (5)	$0.34	$0.24	$0.31	$0.42

(1) The Company recognized approximately $7,000 in store closure and exit costs during the thirteen weeks ended April 27, 2014 with $6,600 associated with the recognition of certain lease liabilities, severance, loss on disposal of assets and other exit costs. The Company also incurred charges of approximately $400 related to the liquidation of inventory.

(2) The Company recognized approximately $9,800 in store closure and exit costs during the thirteen weeks ended July 27, 2014.

(3) The Company recognized a net benefit of approximately $2,900 during the thirteen weeks ended October 26, 2014, related to a gain on the assignment of a capital lease for one of the stores closed in fiscal 2014 and changes in estimates related to its lease commitments for closed stores.

The Fresh Market, Inc.

Notes to the Consolidated Financial Statements (continued)

15. Select Quarterly Financial Data (unaudited) (continued)

(4) The Company recognized approximately $10,600 in charges during the thirteen weeks ended January 25, 2015, including approximately $9,000 in impairment charges of certain store related assets offset by a net reduction in previously closed store expense and approximately $2,100 in charges related to the leadership change during the thirteen weeks ended January 25, 2015.

(5) The net income per share totals may not equal the sum of the components due to rounding.

	Year Ended January 26, 2014			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter (1)
Sales	$366,626	$354,764	$364,457	$425,810
Gross profit	$129,337	$121,278	$122,057	$142,684
Income from operations	$35,384	$25,912	$18,894	$3,191
Net income	$22,120	$15,634	$11,064	$1,989
Net income per share:				
Basic and diluted	$0.46	$0.32	$0.23	$0.04

(1) The Company recognized approximately $27,600 in charges during the thirteen weeks ended January 26, 2014, associated primarily with the impairment of certain real estate and store related assets and the write off of capitalized expenses for real estate sites prior to leasing them.

16. Subsequent Event

On March 5, 2015, the Company announced the closing of its three stores in California. The decision to close these stores followed careful consideration of expected future cash flows, the long-term strategic importance of individual stores, and the anticipated timeline of store openings in California. The Company concluded that the pace of organic store growth was going to be slower than anticipated and believes it can achieve more consistent financial results and a better return on its investments by continuing to grow in markets within or closer to its existing markets at this time.

The Company expects to incur approximately $20,000 to $26,000 in pre-tax charges related to disposals of store assets, which includes leasehold improvements and inventory, the recognition of lease obligations, employee severance costs, store closure and exit activities, and other miscellaneous expenses in future periods. The Company expects store closure activities to be completed in fiscal 2015.