PINK OTC MARKETS ANNUAL REPORT

Phoenix Footwear Group, Inc.

(Report prepared on April 25, 2017 for the 52-week period ended December 31, 2016)

All information contained in this Annual Report has been compiled to fulfill the OTC Pink Basic Disclosure Guidelines to qualify for the OTC Pink Current Information tier.

1) Name of the Issuer and its predecessors (if any).

Phoenix Footwear Group, Inc. (herein referred to as the "Issuer" or "Company"), incorporated in the State of Delaware.

2) Address of the Issuer's principal executive offices:

Company Headquarters

5937 Darwin Court, Suite 109
Carlsbad, CA 92008
Telephone: (760) 602-9688
Facsimile: (760) 602-9619
www.phoenixfootwear.com
www.softwalkshoes.com
www.trotters.com

Investor relations Contact:

Greg W. Slack
5937 Darwin Court, Suite 109
Carlsbad, CA 92008
(760) 602-9688
E-mail: gslack@phxg.com

3) Security Information

Trading Symbol: PXFG
Exact title and class of securities outstanding: Phoenix Footwear Group, Inc. common stock
CUSIP: 71903M209
Par or stated value: $0.01 per share
Total shares authorized: 50,000,000 common shares, as of April 25, 2017
Total shares outstanding: 12,488,362 common shares, as of April 25, 2017

Transfer Agent

Computershare Investor Services
P.O. Box 43078
Providence, RI 02940-3078
(877) 282-1168

Is the Transfer Agent registered under the Exchange Act? Yes: X No: __

List any restrictions on the transfer of security: The Company's common stock is generally subject to securities laws restrictions on transfer. As described below in the footnotes under section "8)c, Beneficial Shareholders", the Greenwood Notes (defined below) issued by the Company to the Greenwood Investors (defined below), and the underlying shares, are restricted from transfer, and contain a customary restrictive legend. In addition, in accordance with the 2011 Plan (defined below), the Company has issued restricted stock certificates to its non-employee directors which contain a customary restrictive legend and are restricted from transfer subject to compliance with securities laws.

As described below under section "4) Issuance History," the Company completed a private placement of $2,000,000 of its common stock in 2015, in a transaction exempt from registration under Rule 506(c) of Regulation D of the Securities and Exchange Act. The shares issued in that transaction were not registered under the Securities Act, and the shares may not be re-offered or re-sold in the United States absent registration or an applicable exemption from registration requirements. Certificates representing the shares issued contained customary restrictive legends and were issued to the Greenwood Investors (defined below) and eligible shareholders who are accredited investors.

Describe any trading suspension orders issued by the SEC in the past 12 months. None.

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off or reorganization either currently anticipated or that occurred within the past 12 months. None.

4) Issuance History

For the previous two fiscal years ended December 31, 2016 and January 2, 2016, and up to the filing of this Annual Report, there have been the following events that resulted or could have resulted in changes in total shares outstanding by the issuer:

On April 1, 2016, the Company issued an aggregate of 70,000 shares of restricted common stock to four non-employee directors, Steven DePerrior, Stephanie Pianka, Frederick Port, and David Whalen in transactions exempt from registration pursuant to Rule 701 under the Securities Act, pursuant to awards granted under the 2011 Long-Term Incentive Plan of Phoenix Footwear Group, Inc. (the "2011 Plan"), upon the satisfaction of vesting criteria which required that the recipients maintain continued membership on the Company's Board of Directors through March 31, 2017. The shares are restricted from transfer unless in compliance with applicable securities laws and the certificates representing the shares contain a customary restrictive legend.

On August 18, 2015, the Company completed the sale of 4,000,000 shares of its common stock at a price of $0.50 per share. The sale was made in a private placement offer to its shareholders who are "accredited investors."

The offering was made directly on a best efforts basis without an underwriter or any minimum number of shares that must be sold. The offering commenced on July 28, 2015, and terminated at 5:00 p.m. Eastern Time on August 17, 2015. The shares were issued to accredited investors in private transactions not involving any public offering and exempt from the registration requirements of the Securities Act pursuant to Section 4(a)(2) thereof, and Rule 506(c) of Regulation D thereunder. The offering was open to all shareholders of record as of June 11, 2015, who are accredited investors and currently reside in the United States.

Greenwood Capital, LP, a Massachusetts limited partnership, and MGPLA, L.P., a Delaware limited partnership, both managed by Greenwood Investments, Inc. (the "Greenwood Investors") purchased 3.2 million shares. 800,000 shares were also purchased by other eligible stockholders, including the Company's Chairman and CEO, James R. Riedman, who purchased 300,000 shares. The shares issued in the offering were not registered under the Securities Act, and the shares may not be re-offered or re-sold in the United States absent registration or an applicable exemption from registration requirements. Certificates representing the shares issued contained customary restrictive legends and were issued to the Greenwood Investors and other eligible shareholders.

On April 1, 2015, the Company issued an aggregate of 60,000 shares of restricted common stock to three non-employee directors, Steven DePerrior, Stephanie Pianka and Frederick Port, in transactions exempt from registration pursuant to Rule 701 under the Securities Act, pursuant to awards granted under the 2011 Long-Term Incentive Plan of Phoenix Footwear Group, Inc. (the "2011 Plan"), upon the satisfaction of vesting criteria which required that the recipients maintain continued membership on the Company's Board of Directors through March 31, 2015. The shares are restricted from transfer unless in compliance with applicable securities laws and the certificates representing the shares contain a customary restrictive legend.

With the exception of the offerings and issuances described above, there have been no securities offerings and share issuances for services of the Company's securities in the previous two fiscal years ended December 31, 2016, and January 2, 2016, or in the interim period following fiscal year ended December 31, 2016, to the date of this Pink OTC Markets Annual Report.

5) Financial Statements

The following audited consolidated financial statements are attached at the end of this Annual Report as Exhibit A and management's discussion and analysis as Exhibit B are attached at the end of this Annual Report and are hereby incorporated by reference:

1. Independent Auditors' Report.
2. Audited Consolidated Balance Sheets as of December 31, 2016, and January 2, 2016.
3. Audited Consolidated Statements of Operations for the fiscal years ended December 31, 2016, and January 2, 2016.
4. Audited Consolidated Statements of Stockholders' Equity for the fiscal years ended December 31, 2016, and January 2, 2016.
5. Audited Consolidated Statements of Cash Flows for the fiscal years ended December 31, 2016, and January 2, 2016.
6. Notes to the Audited Consolidated Financial Statements.
7. Financial Statement Schedule II Consolidated Valuation and Qualifying Accounts.
8. Management's Discussion and Analysis of Financial Condition and Results of Operations as of and for the fiscal years ended December 31, 2016, and January 2, 2016.

6) Describe the Issuer's Business, Products and Services

A. **Description of the Issuer's business operations:**

The Company specializes in quality comfort women's footwear. The Company designs, develops, markets and sells footwear in a wide range of sizes and widths under the brands Trotters® and SoftWalk®. The Company has been engaged in the manufacture or importation and sale of quality footwear since 1882.

Trotters and SoftWalk are the Company's two core brands, which make up its women's footwear business. These products are designed for fit, quality and value for the consumer. The Company specializes in comfort footwear and manufactures each style in a large range of sizes and widths to ensure proper fit. The Company maintains an "open stock" inventory, which provides our customers with the ability to replenish their inventory at retail and support special consumer orders.

B. **Date and State (or Jurisdiction) of Incorporation**:

Phoenix Footwear Group, Inc. was incorporated under the laws of the State of Delaware on March 15, 2002.

C. **The Issuer's primary and secondary SIC Codes**: The Company's primary SIC Code is 3140 - Footwear, except rubber

D. **The Issuer's fiscal year end date:**

The Company's operating and reporting period is on a 52-53 week fiscal year ending on the Saturday nearest to December 31.

E. **Principal products or services, and their markets**:

The Company's products emphasize quality, fit and comfort with classic styling. These products compete predominately in the moderate-priced categories of the market.

Trotters. Competing primarily in the traditional women's dress, tailored and casual classifications, Trotters provides retail price points from $79 to $129. The broad selection of sizes and widths for this brand fills an important need for the Company's customers by emphasizing quality and fit with the continuity of style from season to season.

SoftWalk. SoftWalk competes in the women's comfort footwear segment at moderate retail price points from $89 to $159. Utilizing its patented footbed in a number of its own styles which fundamentally differentiates SoftWalk from its competitors, the Company believes SoftWalk's consumer acceptance and popularity is attributable, in part, to its unique combination of comfort and contemporary styling. The Company's patented footbed technology provides the consumer with exceptional comfort without compromising style and is utilized in many of its SoftWalk products.

During the fiscal years ended December 31, 2016, ("fiscal 2016") and January 2, 2016, ("fiscal 2015"), the Company had one reportable segment consisting of its continuing operations of Trotters and SoftWalk.

Distribution Methods of Issuer's Products

Trotters and SoftWalk products are sold by the Company's own dedicated employee sales force that covers the U.S. market. Beginning in April of 2013, the Company entered into a three year licensing agreement (the "ABC Studios Licensing Agreement") with Touchstone Television Productions, LLC. ("ABC Studios"), to design, market and distribute footwear for the medical community under the Grey's Anatomy brand. Concurrent with the ABC Studios Licensing Agreement, the Company entered into a three year Joint Marketing Agreement (the "Joint Marketing Agreement") with Barco Uniforms, Inc. ("Barco"). Under the terms of the Joint Marketing Agreement, footwear produced under the ABC Studios Licensing Agreement is sold in the U.S. market by Barco's employed sales force. The Company distributes its products in Canada under an exclusive distribution agreement with Canada Shoe Corp, who is the sole importer and distributor of the Company's Trotters and SoftWalk brands in Canada.

On October 19, 2016, the Company entered into the first Amendment of the ABC Studios Licensing Agreement (the "Amended ABC Studios Licensing Agreement") with ABC Studios extending the term an additional three years expiring on December 31, 2019.

Historically, a majority of the Company's revenue is generated by the sale of women's footwear. Some of these styles have been produced under the ABC Studios Licensing Agreement. Under the ABC Studios Licensing Agreement, the Company has the right to produce, market, and sell footwear under the Grey's Anatomy by Softwalk trademark. The Amended ABC Studios Licensing Agreement guarantees a minimum royalty payment over its three year term expiring on December 31, 2019.

During fiscal 2016, the Company's products were carried by approximately 835 customers in over 1,405 retail locations throughout the United States. The Company's distribution channels include leading specialty and independent retail stores, mail order catalogues, and internet retailers. The Company also operates its own direct to consumer internet retail business for all of its brands. Ten significant customers represented approximately 65% and 64% of net sales from continuing operations for fiscal 2016 and fiscal 2015, respectively. Zappos.com, accounted for 16.2% and 15.2%, of net sales in the 52-week period of fiscal 2016 and 2015, respectively, while Amazon accounted for 10.1% and 11.9% of net sales during fiscal periods 2016 and 2015, respectively.

Consumer Direct

The Company believes its e-commerce web sites complement the Company's existing wholesale business by increasing consumer awareness of the Company's brands. Sales through the Company's internet web sites represented approximately 6.4% and 3.5% of its net sales for the 52-week period of fiscal 2016 and fiscal 2015, respectively. The products marketed through the Company's web sites are sold at their suggested retail price, enabling the Company to maintain the full retail margins on in-line products. The Company's footwear can be purchased at *www.SoftWalkshoes.com* and *www.Trotters.com*.

Competitive business conditions, the Issuer's competitive position in the industry, and methods of competition.

The Company faces intense competition in the footwear industry from numerous domestic and foreign designers and marketers. Many of the Company's competitors have greater financial, distribution or marketing resources than the Company, as well as greater brand recognition. Important elements of competition in the footwear industry include:

- anticipating and responding to changing consumer demands in a timely manner;
- maintaining brand reputation and authenticity;
- developing high quality products that appeal to consumers;
- appropriately pricing products;
- providing strong and effective product marketing support;

- ensuring product availability; and
- maintaining and effectively accessing the Company's distribution channels.

Trotters primarily competes with the Naturalizer®, EasySpirit®, Munro America® and Cobb Hill® brands, as well as with retailers' private label footwear. SoftWalk primarily competes with the Sofft®, Born®, Dansko®, and Allegria® brands.

The Company believes that all of its brands are positioned to compete effectively in the footwear industry. By emphasizing traditional style, quality and fit, the Company believes these product lines will continue to maintain a loyal consumer following that is less susceptible to fluctuations due to changing fashions and changes in consumer preferences.

Product Development

The Company has a team of development specialists who commercialize product designs and procure footwear that adheres to the Company's fit, quality and construction standards. They closely manage the production and quality processes with the Company's independent manufacturers in China to ensure timely delivery of goods to the marketplace. The development and commercialization of new product designs include capital outlays for the tooling of dies, molds and lasts, the costs of which are amortized into cost of goods sold over a twelve month period beginning in the season the new design is first distributed. The Company incurred product design and development costs of approximately $380,000 and $334,000 during fiscal 2016 and 2015, respectively. The increase in product development costs is mostly related to the addition of a consultant to design for the Company's Grey's Anatomy line.

Sources and availability of raw materials and the names of principal suppliers.

Factories. The Company's footwear is produced by independent contract manufacturers located in China and Vietnam. The Company does not own or operate any manufacturing facilities. The Company believes that the use of independent manufacturers increases its production flexibility and capacity while substantially reducing capital expenditures and avoiding the costs of managing a large production work force.

In an effort to ensure continuity of product quality and fit, as well as control of production costs, the Company uses manufacturers the Company has previous experience with when possible. The Company attempts to ensure that no one manufacturer is responsible for a disproportionate amount of its merchandise and allocates production between factories to achieve a balance between quality, cost and capability. The Company does not have any long-term contracts with any of its manufacturers; however, the Company has long-standing relationships with its manufacturers and believes its relationships are good.

Production Oversight. To maintain product quality and consistency, the Company oversees the key steps of production from manufacturing of initial prototypes to final manufacturing runs. Monitoring of all production is performed by the Company's in-house production team in the U.S., with closer inspection from its staff located in China. The Company believes this local presence allows it to negotiate supplier and manufacturer arrangements more effectively, decrease product turnaround time, manage quality control and ensure prompt delivery of finished footwear.

Quality Control. Quality control is an important and effective means of maintaining the high standards and reputation of the Company's products. The Company's staff in China performs multiple inspection procedures at various stages of the production process. These include examining key raw materials prior to manufacture, samples and materials at various stages of production and final products prior to shipment. The Company's staff is often on site at each of its manufacturers to oversee production.

Third party manufacturers located in China and Vietnam have produced 100% of the Company's footwear products over the last three fiscal years. The Company depends on the ability of these manufacturers to finance the production of goods ordered, maintain adequate manufacturing capacity and meet the Company's quality standards. The Company competes with other companies for the production capacity of these third party manufacturers, and the Company does not exert direct control over the manufacturers' operations. As such, the Company has experienced at times, delays or inabilities to fulfill customer demand and orders. The Company cannot guarantee that any third party manufacturer will have sufficient production capacity, meet the Company's production deadlines or meet its quality standards.

In addition, from time to time, these manufacturers may and have terminated their relationship with the Company. As a result, the Company is not always assured of an uninterrupted supply of products of an acceptable quality and price from its third party manufacturers. Any disruption in the supply of products from the Company's third party manufacturers may harm its business and could result in a loss of sales and an increase in production costs, which would adversely affect the Company's results of operations.

The Issuer's dependence on one or a few major customers.

Ten significant customers represented approximately 65% and 64% of net sales from operations for the 52-week period of fiscal 2016 and 2015. Zappos.com accounted for 16.2% and 15.2% of net sales in the 52-week period of fiscal 2016 and fiscal 2015, respectively, while Amazon accounted for 10.1% and 11.9% of net sales during the same periods.

Although the Company has enjoyed long-term relationships with many of its customers, they do not have a contractual obligation to purchase the Company's products. The Company cannot be certain that it will be able to retain its existing major customers. The retail industry can be uncertain due to changing customer buying patterns and consumer preferences. These factors could cause the Company to lose one or more of these customers, which could adversely affect its business.

Patents, trademarks, licenses, franchises, concessions, royalty agreements or labor contracts.

The Company regards its proprietary rights as valuable assets and important to its competitive advantage. The Company's trademarks which have been registered in the U.S. and a number of foreign countries include; Trotters and SoftWalk. The Company's SoftWalk brand contains a proprietary technology in the footbed of the shoe, for which the Company owns a patent in the U.S. The Company vigorously protects its intellectual property against infringement. The Company's patents expire at various times through August 2020. The Company cannot be sure, however, that its activities do not, and will not, infringe on the proprietary rights of others.

The need for any government approvals of principal products or services.

The Company is subject to various laws, ordinances and regulations, including those relating to the general operation of a business. The Company believes that it is in compliance with all laws, ordinances and regulations which have a material effect on the operation of its business. The Company is currently not aware of any need for government approval of its principal product or services.

7) Describe the Issuer's Facilities

The general location, use and approximate size of the Company's principal properties are set forth below:

Facility/Location	Own/Lease	Description	Approximate Square Footage
Carlsbad, California	Lease	Office Space	5,195
Old Town, Maine	Lease	Warehouse	75,000
Dongguan, People's Republic of China	Lease	Office Space	2,000
Dolgeville, New York	Own	Vacant Land	30 acres

The Company leases facilities under operating lease agreements expiring through June 2023. The Company's corporate headquarters are located in Carlsbad, California and consists of approximately 5,195 square feet. The lease expires in October 2017.

The Company also leases land and a warehouse located in Old Town, Maine. The lease of the Old Town, Maine Warehouse expires in June 2023.

The company also leases office space in Dongguan, China, to maintain staff overseas to oversee its manufacturing operations in China.

The Company believes that its current facilities are in good operating condition and are adequate for its current and foreseeable future operating requirements.

8) Officers, Directors, and Control Persons

A. Names of Officers, Directors, and Control Persons.

The names of each of the Company's executive officers, directors and control persons as of the date of this Annual Report are as follows:

Executive Officers:

James R. Riedman, Chairman, President and Chief Executive Officer
Bruce Kaplan, Executive Vice President
Greg W. Slack, Chief Financial Officer, Treasurer and Secretary

Directors:

James R. Riedman
Steve M. DePerrior
Frederick R. Port
Stephanie E. Pianka
David G. Whalen

Control Persons (defined as beneficial owners of more than five percent of the Company's common stock):

Riedman Corporation and James R. Riedman
Greenwood Investments, Inc. and Steven Tannenbaum
Greenwood Capital LP

For additional information pertaining to the number of shares of common stock beneficially owned by persons known to the Company to beneficially own more than ten percent (10%) of the outstanding shares of common stock as of April 25, 2017, see the discussion included in section 8) (C) below under the subheading "Beneficial Shareholders."

B. Legal/Disciplinary History

None of the Company's directors, executive officers or control persons were convicted in a criminal proceeding during the past five years or have been named as a defendant in a pending criminal proceeding. Additionally, none of these persons were a party to any judicial, self-regulatory organization, or other administrative proceeding during the past five years that resulted in a judgment, decree or final order barring, enjoining, suspending or otherwise limiting such persons involvement in any type of business, securities, commodities or banking activities or enjoining the person from future violations of, or prohibiting activities subject to, federal or state securities or commodities laws, or a finding of any violation of federal or state securities or commodities laws.

C. Beneficial Shareholders

The following table shows the number of shares of common stock beneficially owned by persons known to the Company to beneficially own more than ten percent of the outstanding shares of common stock as of April 25, 2017. For the purposes of computing a person's beneficial ownership, shares of common stock issuable upon the exercise of securities exercisable or convertible into common stock within 60 days of April 25, 2017, are deemed outstanding for the purposes of computing the share ownership and percentage ownership of the person holding such securities, but are not deemed outstanding for the purposes of computing the percentage ownership of any other person.

Percentage of beneficial ownership is calculated assuming 12,488,362 shares of the Company's common stock (net of treasury shares) were outstanding as of April 25, 2017. Except as otherwise indicated, to the Company's knowledge, the beneficial owners of common stock listed below have sole or shared investment and voting power with respect to such shares.

Beneficial Owners of 10% or More	Amount and Nature of Beneficial Ownership (1)	Percent of Class
James R. Riedman and Riedman Corporation (2), (3), (4)	13,414,002	71.5%
Greenwood Investments, Inc. and Steven Tannenbaum (2), (3), (4)	13,414,002	71.5%

(1) Unless otherwise noted, and subject to applicable community property laws, each person has sole or shared voting and dispositive power with respect to all shares of common stock beneficially shown as owned by that person.

(2) Includes 1,261,600 shares owned directly, 350,000 shares underlying outstanding stock options held by Mr. Riedman, 443,808 owned indirectly through CE Capital, LLC, an affiliated entity, and the following shares and shares issuable upon exercise of outstanding stock options of which Mr. Riedman disclaims beneficial ownership: 382,710 shares and 50,000 shares underlying outstanding stock options beneficially owned by Riedman Corporation, of which Mr. Riedman is a director and a shareholder; 87,337 shares owned by his children; and 139,975 shares held by the Company's 401(k) Plan, not including 16,957 shares allocated to his account. Mr. Riedman is a member of the Board's Retirement Plan Committee, which serves as fiduciary for the Company's 401(k) Plan, and through that committee he shares voting control over such shares. The plan's mailing address is c/o Phoenix Footwear Group, Inc., 5937 Darwin Court, Suite 109, Carlsbad, California 92008. Riedman Corporation acts as its own resident agent and may be contacted at 45 East Avenue, Rochester, New York 14604. The name and address of the General Partner's resident agent is Incorporating Services, Ltd., 3500 Dupont Hwy, Dover, Delaware 19901.

.(3) Includes: (i) 4,812,050 shares of common stock owned by Greenwood Capital, LP; and (ii) 5,869,565 of common stock issuable upon conversion of three promissory notes held by Greenwood Capital, LP in the aggregate original principal amount of $1,350,000 (the "Greenwood Notes"). Also, includes shares held by James Riedman and Riedman Corporation (collectively the "Riedman Shareholders"), that may be deemed to be beneficially owned by Greenwood Capital, LP under the Voting Agreement as described in Note 4 below. Greenwood Investments, Inc. is the general partner of the Greenwood Capital, LP., and has the authority to vote and dispose of all of the shares held. Steven Tannenbaum is the president of Greenwood Investments, Inc., Greenwood Capital, LP, Greenwood Investments, Inc., and Mr. Tannenbaum (collectively the "Greenwood Parties"). Each have a principal business address at Prudential Tower, 800 Boylston Street, Suite 1450, Boston, MA 02199.

(4) In connection with the purchase of the Greenwood Notes, the Greenwood Parties entered into a Voting Agreement on July 21, 2011 with the Riedman Shareholders and the Company, as amended on July 23, 2015 (the "Voting Agreement"). The Voting Agreement provides, among other things for the parties to vote on one candidate of the Riedman Shareholders and one candidate of the Greenwood Parties as directors of the Company's Board of Directors. As a result of the Voting Agreement and as of the date hereof, (i) the Riedman Shareholders may be deemed to beneficially own 10,681,615 shares beneficially owned by the Greenwood Parties and (ii) the Greenwood Parties may be deemed to beneficially own 2,732,387 shares beneficially owned by the Riedman Shareholders. Both the Riedman Shareholders and Greenwood Parties expressly disclaim being a member of a Section 13(d)(3) "group" with any of the reporting persons of the other party, and further expressly disclaim and beneficial ownership of the shares of the other.

9) Third Party Providers

There are no outside providers that advise the issuer on matters relating to the operations or business development of the Company.

Legal Counsel:

Woods Oviatt Gilman LLP
700 Crossroads Building
2 State Street
Rochester, NY 14614
(585) 987-2800
administrator@woodsoviatt.com

Woods Oviatt Gilman, LLP has been engaged by the Company to review certain legal matters in connection with management's preparation of this disclosure statement.

Accountant: Mayer Hoffman McCann P.C.
10616 Scripps Summit Court
San Diego, CA 92131
(858) 795-2017
Stuart Starr, Engagement Partner
sstarr@cbiz.com

Mayer Hoffman McCann P.C. ("MHM") is an independent registered public accounting firm who has audited the Company's books and accounts for fiscal 2015 and fiscal 2016, which were prepared by the Company's management, including its Chief Financial Officer. MHM's audits are conducted in accordance with auditing standards generally accepted in the United States of America. Those standards require MHM to plan and perform their audit to obtain reasonable assurance about whether the Company's financial statements are free of material misstatements. MHM's audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements including assessing the accounting principles used and significant estimates made by the Company, as well as evaluating the overall financial statement presentation. The preparation of the consolidated financial statements, financial schedules and footnotes are the responsibility of the Company.

Except as noted above, there are no other outside advisors that assisted, advised, prepared or provided information with respect to this disclosure statement.

10) Issuer Certifications

I, James R. Riedman, President and Chief Executive Officer, certify that:

1. I have reviewed this annual disclosure statement of Phoenix Footwear Group, Inc.;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

April 25, 2017

/s/ James R. Riedman
President and Chief Executive Officer

I, Gregory W. Slack, Chief Financial Officer, Secretary and Treasurer, certify that:

1. I have reviewed this annual disclosure statement of Phoenix Footwear Group, Inc.;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

April 25, 2017

/s/ Gregory W. Slack
Chief Financial Officer, Secretary and Treasurer

Exhibit A

PHOENIX FOOTWEAR GROUP, INC.

AUDITED FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2016

Audited Financial Statements

Mayer Hoffman McCann P.C.
An Independent CPA Firm

10616 Scripps Summit Court
San Diego, California 92131
858-795-2000 ph
858-795-2001 fx
www.mhm-pc.com

Independent Auditors' Report

To the Board of Directors and Stockholders of
Phoenix Footwear Group, Inc.
Carlsbad, California

We have audited the accompanying consolidated financial statements of **Phoenix Footwear Group, Inc.** (a Delaware corporation), which comprise the consolidated balance sheets as of **December 31, 2016** and **January 2, 2016** and the related consolidated statements of income, stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements. Our audit also included the financial statement schedule listed in **Section 5**.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of **Phoenix Footwear Group, Inc.** as of **December 31, 2016** and **January 2, 2016** and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedule referred to above, presents fairly, in all material respects, the information set forth therein.

/s/ Mayer Hoffman McCann P.C.
San Diego, CA
April 25, 2017

PHOENIX FOOTWEAR GROUP, INC.

CONSOLIDATED BALANCE SHEETS
(In thousands, except for per share data)

	December 31, 2016	January 2, 2016
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 342	$ 283
Accounts receivable (less allowances of $1,493 and $1,281 in 2016 and 2015, respectively)	2,096	2,812
Inventories (less provision of $417 and $493 in 2016 and 2015, respectively)	9,160	10,363
Other current assets	557	407
Total current assets	12,155	13,865
PROPERTY, PLANT AND EQUIPMENT, net	35	54
Capital leased asset, net	440	515
OTHER ASSETS	109	161
TOTAL ASSETS	$ 12,739	$ 14,595
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Revolving line of credit and note payable, current (Note 5)	$ 4,424	$ 5,156
Accounts payable	3,362	2,974
Accrued expenses	904	805
Current portion of long term debt	427	446
Total current liabilities	9,117	9,381
OTHER LONG-TERM LIABILITIES		
Term notes payable, net of current portion (Note 5)	97	444
Convertible notes payable	1,350	1,350
Capital lease obligation, net of current portion	451	502
Other non-current liabilities	146	198
Total liabilities	11,161	11,875
Commitments and contingencies (Note 3)		
STOCKHOLDERS' EQUITY:		
Common stock, $0.01 par value — 50,000 shares authorized; 12,705 and 12,635 shares issued and outstanding in 2016 and 2015	128	127
Additional paid-in-capital	48,205	48,152
Accumulated deficit	(44,112)	(42,916)
Treasury stock at cost, 217 shares in 2016 and 2015	(2,643)	(2,643)
Total stockholders' equity	1,578	2,720
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 12,739	$ 14,595

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

PHOENIX FOOTWEAR GROUP, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Year Ended	
	December 31, 2016	January 2, 2016
Net sales	$ 20,244	$ 21,655
Cost of goods sold	12,817	14,374
Gross profit	7,427	7,281
Operating expenses:		
Selling, general and administrative	8,058	7,537
Total operating expenses	8,058	7,537
Operating loss	(631)	(256)
Interest expense, net	590	776
Loss before income taxes	(1,221)	(1,032)
Income tax benefit (expense)	25	—
Net loss	$ (1,196)	$ (1,032)
Net loss per share:		
Basic	$ (0.10)	$ (0.11)
Diluted	(0.10)	(0.11)
Net loss per share	$ (0.10)	$ (0.11)
Weighted average shares outstanding used to calculate per share information:		
Basic	12,471	9,553
Diluted	12,471	9,553
Net loss	$ (1,196)	$ (1,032)

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

PHOENIX FOOTWEAR GROUP, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands)

	Common Stock		Additional Paid-In Capital	Accumulated Deficit	Treasury Stock		Total
	Shares	Amount			Shares	Amount	
Balance — January 3, 2015	8,575	$ 87	$ 46,179	$ (41,884)	(217)	$ (2,643)	$ 1,739
Issuance of common stock	4,060	40	1,906	—	—	—	1,946
Stock-based compensation for services	—	—	67	—	—	—	67
Net loss	—	—	—	(1,032)	—	—	(1,032)
Balance — January 2, 2016	12,635	$ 127	$ 48,152	$ (42,916)	(217)	$ (2,643)	$ 2,720
Issuance of common stock	70	1	—	—	—	—	1
Stock-based compensation for services	—	—	53	—	—	—	53
Net loss	—	—	—	(1,196)	—	—	(1,196)
Balance — December 31, 2016	12,705	$ 128	$ 48,205	$ (44,112)	(217)	$ (2,643)	$ 1,578

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

PHOENIX FOOTWEAR GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	For the Fiscal Years Ended	
	December 31, 2016	January 2, 2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (1,196)	$ (1,032)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	94	100
Provision for losses on accounts receivable	213	172
Non-cash stock-based compensation	54	108
Amortization of deferred debt issuance costs	57	130
Changes in assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	503	(535)
Inventories, net	1,203	(2,213)
Other current assets	(154)	139
Income taxes receivable	(1)	(12)
Increase (decrease) in:		
Accounts payable	388	373
Accrued expenses	100	(332)
Other long-term liabilities	(51)	(33)
Net cash provided by (used in) operating activities	1,210	(3,135)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of equipment	—	(7)
Net cash used in investing activities	—	(7)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings on line of credit	19,822	24,623
Payments of line of credit	(20,555)	(22,299)
Payments of notes payable and capital lease	(418)	(871)
Issuance of common stock, net of issuance costs	—	1,905
Payment of debt issuance costs	—	(261)
Net cash (used in) provided by financing activities	(1,151)	3,097
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	59	(45)
CASH AND CASH EQUIVALENTS — Beginning of period	283	328
CASH AND CASH EQUIVALENTS — End of period	$ 342	$ 283
SUPPLEMENTAL CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest	455	650
Income taxes	25	23
Supplemental disclosure of non-cash financing activities:		
Issuance of restricted stock grants	53	41
Capital lease obligation	—	64

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

PHOENIX FOOTWEAR GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

Definitions

As used in this report, unless the context suggests otherwise, "Phoenix Footwear," "the Company," "its", "our," "us", and "we" means Phoenix Footwear Group, Inc. and its consolidated subsidiary, Penobscot Shoe Company, "the FASB" means the Financial Accounting Standards Board, "SFAS" means Statement of Financial Accounting Standards, "ASC" means the "FASB Accounting Standards Codification™", "ASU" means "Accounting Standards Update" and "SEC" means the Securities and Exchange Commission.

Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP").

Accounting Period

The Company's operating and reporting period is on a 52-53 week fiscal year ending on the Saturday nearest to December 31. The Company refers to the fiscal year ended January 2, 2016, as "fiscal 2015," the fiscal year ending December 31, 2016 as "fiscal 2016," and the fiscal year ending December 30, 2017, as "fiscal 2017." The 52-week fiscal years consist of four equal quarters of 13 weeks each, and the 53-week fiscal years consist of three 13-week fiscal quarters and one 14-week fiscal quarter. The financial results for the 53-week fiscal years and 14-week fiscal quarters will not be exactly comparable to the 52-week fiscal years and 13-week fiscal quarters. Fiscal 2016, ended December 31, 2016, and fiscal 2015, ended January 2, 2016, each included 52 weeks.

Principles of Consolidation

The consolidated financial statements consist of Phoenix Footwear Group, Inc. and its wholly-owned subsidiary, Penobscot Shoe Company. Intercompany accounts and transactions have been eliminated in consolidation.

Management Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Management believes that the estimates, judgments and assumptions made when accounting for items and matters such as, but not limited to, the allowances for doubtful accounts, sales returns, impairment assessments and charges, recoverability of assets (including deferred tax assets), uncertain tax provisions, share-based compensation expense, the assessment of lower of cost or market on inventory, useful lives assigned to long-lived assets, and depreciation are reasonable based on the information available at the time they were made. Management also makes estimates in the assessments of potential losses in relation to tax matters, and threatened or pending legal proceedings. Actual results could materially differ from those estimates. For matters not related to income taxes, if a loss is considered probable and the amount can be reasonably estimated, the Company recognizes an expense for the estimated loss. If there is the potential to recover a portion of the estimated loss from a third party, management makes a separate assessment of recoverability and reduces the estimated loss if the recovery is deemed probable.

Segments

The Company determines operating segments on the same basis that it evaluates the performance internally. The operating segments have been aggregated and are reported as one reportable financial segment. The Company aggregates its operating segments for financial reporting purposes because they are similar in each of the following areas: economic characteristics; type of customer; nature of products; nature of production processes; and distribution methods.

The Company had only one reportable segment in both fiscal 2016 and 2015 consisting of Trotters and SoftWalk.

Business and Credit Concentrations

The Company maintains cash in U.S. bank accounts which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant cash risk.

The Company sells much of its footwear to 835 customers across the United States, comprised of leading specialty and independent retail stores, mail order catalogues, uniform, and internet retailers. A decision by the controlling owner of a group of stores or any significant customer to decrease the amount of merchandise purchased from the Company or to cease carrying the Company's products could have an adverse effect on the Company's results of operations in future periods. Additionally, the financial difficulties of a customer could cause the Company to curtail business with that customer or the customer to reduce its business with the Company and cancel orders. Ten significant customers represented approximately 65% and 64% of our net sales from continuing operations in fiscal 2016 and fiscal 2015, respectively, including one customer, which comprised 16.2% and 15.2% of net sales in fiscal 2016 and fiscal 2015, respectively.

The Company extends credit to these customers based on an evaluation of each customer's financial condition. The Company monitors its exposure for credit losses on all receivables and maintains allowances for anticipated losses. Credit risk is impacted by conditions or occurrences within the economy and the retail industry and is principally dependent on each customer's financial condition. Four of the Company's customers constituted 59% of trade accounts receivable outstanding at December 31, 2016. The Company's inability to collect on its trade accounts receivable from any of its major customers could adversely affect the Company's results of operation and financial condition.

The Company currently buys all its products from seven independent contract manufacturers located in China and Vietnam. As of December 31, 2016, four of the Company's vendors constituted 89% of its accounts payable. The Company does not have long-term written agreements with any of its manufacturers. The Company could experience difficulties with these manufacturers, including reductions in the availability of production capacity, failure to meet the Company's quality control standards, failure to meet production deadlines or increased manufacturing costs. If the Company's current manufacturers cease doing business with it, the Company could experience an interruption in the manufacture of the Company's products. Although the Company believes that it could find alternative manufacturers, the Company may be unable to establish relationships with alternative manufacturers that will be as favorable as the relationships that exist currently. If the Company is unable to provide products consistent with its standards or the manufacture of the Company's footwear is delayed or becomes more expensive, this could result in customers canceling orders, refusing to accept deliveries or demanding reductions in purchase prices, any of which could have a material adverse effect on the Company's business and results of operations. In addition, the Company's operations are subject to the customary risks of doing business abroad, including but not limited to currency fluctuations and revaluations, custom duties and related fees, various import controls and other monetary barriers, restrictions on the transfer of funds, labor unrest and strikes and, in certain parts of the world, political instability.

Fair Value of Financial Instruments

The Company's financial instruments consist primarily of cash and cash equivalents, accounts and other receivables, accounts payable, accrued expenses, the revolving credit facility and term note and convertible notes. The carrying amount of cash, cash equivalents, accounts receivable, other receivables, accounts payables and accrued liabilities approximates fair value due to the relatively short maturity of such instruments. The carrying amount of the Company's notes payable outstanding under the revolving credit facility, long term notes and convertible notes approximates its fair value based upon current rates and terms available to the Company for similar debt.

Cash Equivalents

The Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

Accounts Receivable

The Company provides a reserve against its accounts receivable for estimated losses that may result from non-collection due to the financial position of its customers. To minimize the likelihood of uncollectibility, customers' credit-worthiness is reviewed periodically based on external credit reporting services and the Company's experience with the account, and is adjusted accordingly. When a customer's account becomes significantly past due, the Company generally places a hold on the account and discontinues further shipments to that customer, minimizing further risk of loss. The Company determines the amount of the reserve by analyzing known uncollectible accounts, aged receivables, historical losses and its customers' credit-worthiness. Amounts later determined and specifically identified to be uncollectible are charged or written off against this reserve. In addition to these individual assessments, in general, outstanding trade accounts receivable amounts that are greater than 365 days are fully reserved for and amounts greater than 120 days are 75% reserved for. The Company's levels of reserves fluctuate depending upon all of the factors mentioned above. The Company also reserves for potential trade discounts and deductions for co-op advertising normally taken by its customers. These trade allowances provided to its retail customers enhances the flow of goods through the retail channels while reducing the level of sales returns.

Historically, actual results in these areas have not been materially different than the Company's estimates, and the Company does not anticipate that its estimates and assumptions are likely to materially change in the future. However, if the Company incorrectly anticipates trends or unexpected events occur, its results of operations could be materially affected.

Inventories and Cost of Goods Sold

Inventories, principally finished goods, are valued at the lower of cost (based on the first-in, first-out method) or market. The cost elements included in inventory consist of all direct costs of products (net of purchase discounts and vendor allowances), allocated overhead (primarily sourcing and indirect production costs), inbound freight and merchandise acquisition costs such as import fees. The Company reduces the carrying cost of inventories for obsolete or slow moving items as necessary to properly reflect inventory value. Reserves are estimated based upon inventory on hand, historical sales activity and the expected net realizable value. The Company's analysis includes a review of inventory quantities on hand at period end in relation to year-to-date sales, existing orders from customers and projections for sales in the near future. The net realizable value, or market value, is determined using the Company's estimate of sales prices of such inventory based upon historical sales experience on a style by style basis or, if necessary, through off-price or discount store channels.

Cost of goods sold includes the inventory cost elements listed above as well as outbound shipping and handling. The Company's cost of goods sold may not be comparable to those of other entities, since some entities include all of the costs associated with their distribution functions in cost of goods sold while the Company includes these costs in SG&A expenses.

Deferred Financing Costs

Deferred financing costs are amortized over the term of the related debt instrument. Amortization expense associated with deferred financing costs is recorded as interest expense and totaled $57,000 and $130,000 in fiscal 2016 and fiscal 2015, respectively. The amortization expense during fiscal 2016 and 2015 is associated with the Company's revolving line of credit with Sterling National Bank (f.k.a: NewStar Business Credit, LLC) and the Economic Recovery Loan Program Loan with the Financial Authority of Maine. Additionally, during 2015, the company incurred $65,000 of additional expense associated with the early acceleration of prepaid debt costs when it terminated the Alostar Loan Agreement in February 2015.

Property, Plant, Equipment, Depreciation and Amortization

Property, plant and equipment are recorded at cost. Repair and maintenance costs that do not improve service potential or extend economic life are expensed as incurred. Depreciation is computed by the straight-line method over the estimated useful lives of the assets. Land is not depreciated, and construction in progress is not depreciated until ready for service. Leasehold improvements recorded at the inception of a lease are amortized using the straight-line method over the life of the lease or the useful life of the improvement, whichever is shorter. For improvements made during the lease term, the amortization period is the shorter of the useful life or the remaining lease term (including any renewal periods that are deemed to be reasonably assured). Property under capital leases is amortized over the lives of the respective leases or the estimated useful lives of the assets, whichever is shorter.

The following tables summarize the Company's major classes of property, plant and equipment and capital leased assets:

	December 31, 2016	January 2, 2016	Useful Lives (Years)
	(In thousands)		
Machinery, furniture and equipment	$ 296	$ 296	4 - 10 years
Leasehold improvements	65	65	2 - 10 years
Computer hardware and software	539	539	2 - 5 years
	900	900	
Less accumulated depreciation and amortization	(865)	(846)	
Property, plant and equipment, net	$ 35	$ 54	

	December 31, 2016	January 2, 2016	Useful Lives (Years)
	(In thousands)		
Capital leased asset (land and building)	$ 684	$ 684	10 years
Less accumulated depreciation and amortization	(244)	(169)	
Capital leased asset, net	$ 440	$ 515	

As described in Note 5, "Debt", on July 1, 2013, the Company completed the sale and contemporaneous leaseback of the land and warehouse facility (collectively, the "Property") located in Old Town, Maine owned by Penobscot Shoe Company, a Maine corporation and wholly owned subsidiary ("Penobscot"), to Old Town Partners, LLC (the "Buyer") pursuant to the terms of a purchase and sale agreement for $620,000. The transaction was accounted for as a capital lease resulting in the recording of a capital leased asset and capital leased obligation equal to the Property's selling price. A gain of $224,000 on the sale of the Property was deferred and is being recognized in proportion to depreciation of the capital leased asset over the initial 10 year term of the lease.

Depreciation associated with the capital lease asset during fiscal 2016 and fiscal 2015 was $75,000 and $76,000, respectively. Depreciation expense specifically associated with the Company's property, plant, and equipment for fiscal 2016 and fiscal 2015 was $19,000 and $24,000, respectively.

Long-lived Assets Impairments

The Company reviews the carrying value of its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. Identification of any impairment would include a comparison of estimated future undiscounted operating cash flows anticipated to be generated during the remaining life of the assets with their net carrying value. An impairment loss would be recognized as the amount by which the carrying value of the assets exceeds their fair value. For fiscal 2016 and fiscal 2015, no impairment loss was recognized as a result of this review.

Revenue Recognition

The Company recognizes revenue from product sales when persuasive evidence of an arrangement exists, products are shipped and the customer takes title and assumes risk of loss, the sales price charged is fixed and determinable and collectability is reasonably assured. Product sales and shipping revenues, net of sales allowances, discounts and return allowances, are recorded when the products are shipped or, in certain situations, upon acceptance by the customer. Allowances for estimated returns are accounted for as reductions to sales, cost of goods sold, accounts receivable and an increase in inventory to the extent such product is resalable. The Company bases its estimates on historical rates of customer returns and allowances, as well as the specific identification of outstanding returns and allowances, which are known to the Company but which have not yet been received or paid. Sales taxes collected from e-commerce customers are excluded from reported sales.

Shipping Activities

Amounts billed to customers related to shipping and handling costs incurred in delivering product to the customer are included in net sales. Related costs incurred are included in cost of goods sold. Shipping and handling costs incurred in bringing products to the Company's warehouse are capitalized as part of inventory. Costs associated with the Company's own distribution and warehousing are recognized as expense as incurred and are included in SG&A.

Product Design and Development Costs

Expenditures relating to the design of new products and processes, including significant improvements and refinements to existing products, are expensed as incurred and included in SG&A. The amounts charged to expense were $380,000 and $334,000 in fiscal 2016 and fiscal 2015, respectively. The increase in product costs is primarily related to a consultant hired during 2016 to focus on the Company's Grey's Anatomy Line.

Advertising Programs

The Company capitalizes direct-response advertising costs when (1) it can be shown that customers responded to a specific advertisement and (2) there is a probable future economic benefit. Direct-response advertising costs, such as those for our catalogues, are capitalized and amortized over their useful lives (generally two to four months). As of December 31, 2016, the Company had no capitalized advertising costs. The Company expenses non direct-response advertising production costs as incurred and records communication costs as an expense when the advertisement first takes place. Catalogue and other advertising costs totaled $450,000 and $298,000 during fiscal 2016 and fiscal 2015, respectively. The increase in advertising expense is due to an increase in other advertising and marketing costs in order to increase the Company's brand recognition.

The Company participates in certain cooperative advertising programs to reimburse a portion of advertising and marketing costs that its customers may incur. Such costs include mailing expenses for catalogues and advertisement runs in newspapers, magazines, radio and television. The Company records cooperative advertising costs as an expense when the advertising first takes place. Total cooperative advertising expense, which was included in SG&A, was $77,000 and $53,000 for fiscal 2016 and fiscal 2015, respectively.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes, in accordance with ASC 740-10, Income Taxes, which requires that the Company recognize deferred tax liabilities for taxable temporary differences and deferred tax assets for deductible temporary differences and operating loss carry-forwards using enacted tax rates in effect in the years the differences are expected to reverse. Deferred income tax benefit or expense is recognized as a result of changes in net deferred tax assets or deferred tax liabilities. A valuation allowance is recorded when it is more likely than not that some or all of any deferred tax assets will not be realized.

The Company applies the provisions of ASC 740-10, which contains a two-step process for recognizing and measuring uncertain tax positions. The first step is to determine whether or not a tax benefit should be recognized. A tax benefit will be recognized if the weight of available evidence indicates that the tax position is more likely than not to be sustained upon examination by the relevant tax authorities. The recognition and measurement of benefits related to the Company's tax positions requires significant judgment, as uncertainties often exist with respect to new laws, new interpretations of existing laws, and rulings by taxing authorities. Differences between actual results and our assumptions or changes in our assumptions in future periods are recorded in the period they become known.

Earnings (Loss) Per Share

Basic earnings per common share is calculated by dividing earnings allocated to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect, in periods in which they have a dilutive effect, the effect of unvested restricted stock not classified as participating securities and common shares issuable upon exercise of stock options or warrants and other convertible securities. The difference between reported basic and diluted weighted-average common shares results from the assumption that all dilutive stock options and warrants and other convertible securities outstanding were exercised and all outstanding restricted shares have vested.

Options, stock rights and convertible notes outstanding to purchase 6,155,042 and 6,493,683 shares of common stock were excluded from the computation of diluted earnings per share for fiscal 2016 and fiscal 2015, respectively, because their inclusion would have been anti-dilutive.

Reconciliation of the numerators and denominators of basic and diluted loss per share for fiscal 2016 and fiscal 2015 is as follows:

	December 31, 2016	January 2, 2015
	(In thousands, except per share data)	
Loss per share from continuing operations, basic and diluted:		
Loss from operations	$ (1,196)	$ (1032)
1% Subordinated convertible notes interest	64	66
Loss adjusted for assumed conversion	$ (1,132)	$ (966)
Basic: Weighted average common shares outstanding	12,471	9,553
Diluted: Weighted average common shares outstanding	12,471	9,553
Loss per share from operations, basic	$ (0.10)	$ (0.11)
diluted	$ (0.10)	$ (0.11)

Recently Adopted Accounting Standards

Debt Issuance Costs

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-03: *Simplifying the Presentation of Debt Issuance Costs,* which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 requires retrospective adoption and is effective for fiscal years beginning after December 15, 2015. In August 2015, the FASB issued ASU 2015-15: *Interest — Imputation of Interest (Subtopic 835-30),* which relates to the presentation of debt issuance costs associated with line-of-credit arrangements. This standard clarifies the guidance set forth in ASU 2015-03, which requires that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from the debt liability rather than as an asset. The new pronouncement clarifies that debt issuance costs related to line-of-credit arrangements could continue to be presented as an asset and be subsequently amortized over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the arrangement. The Company considered this clarification in conjunction with the adoption of ASU 2015-03, which occurred on January 1, 2016. These pronouncements did not have a material impact on the Company's condensed consolidated financial statements. In adopting ASU 2015-15, the Company elected to present debt issuance costs related to line-of-credit arrangements as an asset.

Share-Based Payments

In June 2014, the FASB issued ASU 2014-12 in response to the Emerging Issues Task Force consensus on Issue 13-D. The ASU clarifies that entities should treat performance targets that can be met after the requisite service period of a share-based payment award as performance conditions that affect vesting. Therefore, an entity would not record compensation expense related to an award for which transfer to the employee is contingent on the entity's satisfaction of a performance target until it becomes probable that the performance target will be met. The ASU does not contain any new disclosure requirements. This ASU is effective for all entities for reporting periods (including interim periods) beginning after December 15, 2015. On January 1, 2016, the Company adopted this pronouncement, which did not have a material impact on its consolidated financial statements.

Recently Issued Accounting Standards - Not Yet Adopted

Statement of Cash Flows - Classification

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, which provides guidance for how certain transactions are classified in the statement of cash flows. This standard requires a retrospective transition method to each period presented and is effective for reporting periods beginning after December 15, 2017, with early adoption permitted. The Company is currently assessing the impact of the adoption of this standard on its consolidated financial statements.

Stock Compensation

In March 2016, the FASB issued ASU No. 2016-09, *Compensation — Stock Compensation (Topic 718),* which is intended to increase simplification of accounting for equity share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This standard is effective for annual periods (including interim periods) beginning after December 15, 2016, with early adoption permitted.

Amendments related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements, forfeitures, and intrinsic value should be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. Amendments related to the presentation of employee taxes paid on the statement of cash flows when an employer withholds shares to meet the minimum statutory withholding requirement should be applied retrospectively. Amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement and the practical expedient for estimating the expected term should be applied prospectively. An entity may elect to apply the amendments related to the presentation of excess tax benefits on the statement of cash flows using either a prospective transition method or a retrospective transition method. The Company is currently assessing the impact of adoption of this standard on its consolidated financial statements.

Prepaid Stored-Value Products

In March 2016, the FASB issued ASU No. 2016-04, *Liabilities — Extinguishment of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products.* This update aligns recognition of the financial liabilities related to prepaid stored-value products (for example, prepaid gift cards), with Topic 606, *Revenue from Contracts with Customers*, for non-financial liabilities. In general, certain of these liabilities may be extinguished proportionally in earnings as redemptions occur, or when redemption is remote if issuers are not entitled to the unredeemed stored value. This standard is effective for annual periods (including interim periods) beginning after December 15, 2017, with early adoption permitted. At adoption, this update will be applied either using a modified retrospective transition method by means of a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year in which the guidance is effective or retrospectively to each period presented. The Company is currently assessing the adoption method and the impact that adopting this new accounting standard will have on its consolidated financial statements.

Leases

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842),* which is intended to increase transparency and comparability of accounting for lease transactions. This update revises accounting for operating leases by a lessee, among other changes, and requires a lessee to recognize a liability to make lease payments and an asset representing a company's right to use the underlying asset for the lease term in the balance sheet. The distinction between finance and operating leases has not changed and the update does not significantly change the effect of finance and operating leases on the statement of operations. This standard is effective for annual periods (including interim periods) beginning after December 15, 2019, with early adoption permitted. At adoption, this update will be applied using a modified retrospective approach. The Company is

currently assessing the impact of adoption of this standard on its consolidated financial statements.
Financial Instruments

In January 2016, the FASB issued ASU 2016-01: *Financial Instruments — Overall: Recognition and Measurement of Financial Assets and Financial Liabilities.* The pronouncement requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset, and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The ASU requires the adoption method by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The amendments relating to equity securities without readily determinable fair values (including disclosure requirements) will be applied prospectively to equity investments that exist as of the date of adoption. These changes become effective for fiscal years beginning after December 15, 2017. The expected adoption method is being evaluated by the Company and is not expected to have a significant impact on its consolidated financial statements.

Inventory

In July 2015, the FASB issued ASU 2015-11: *Simplifying the Measurement of Inventory*, which modifies existing requirements regarding measuring inventory at the lower of cost or market. Specifically, this standard eliminates the need to determine and consider replacement cost or net realizable value less an approximately normal profit margin when measuring inventory. This ASU requires a prospective adoption method and is effective prospectively after December 15, 2016, with early adoption permitted. The Company is currently evaluating the impact that this pronouncement will have on its consolidated financial statements.

Revenue Recognition

In May 2014, the FASB issued ASU 2014-09: *Revenue from Contracts with Customers (Topic 606)*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that "an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services." ASU 2014-09 becomes effective for reporting periods (including interim periods) beginning after December 15, 2018. Early application is permitted for reporting periods (including interim periods) beginning after December 15, 2016. This new standard permits the use of either the retrospective or cumulative effect transition method. The Company is currently evaluating the impact that this pronouncement will have on its condensed consolidated financial statements. The Company has not yet selected a transition method or determined the effect of the standard on financial reporting once the standard is effective.

In May 2016, the FASB issued ASU 2016-12: *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*, which provides narrow scope improvements and practical expedients related to ASU 2014-09: *Revenue from Contracts with Customers (Topic 606)*. The purpose of ASU 2016-12 is to clarify certain narrow aspects of Topic 606 such as assessing the collectability criterion, presentation of sales taxes and other similar taxes collected from customers, noncash consideration, contract modifications at transition, completed contracts at transition, and technical correction. The standard has the same effective date as ASU 2014-09 described above. The Company is currently evaluating the impact that this pronouncement will have on its condensed consolidated financial statements. The Company has not yet selected a transition method or determined the effect of the standard on financial reporting once the standard is effective.

2. LIQUIDITY & CAPITAL RESOURCES

Cash and cash equivalents at fiscal 2016 increased to $342,000 compared to $283,000 at fiscal 2015. The cash and cash equivalents balance fluctuates throughout the year due in part to the seasonal change in working capital requirements.

Cash outflows supporting inventory purchasing, selling activities and distribution typically increase from December to February, and again, between June and August each year.

Finance Authority of Maine Term Loan

As describe in Note 8, "Subsequent Events," on April 4, 2017, the Company entered into an Equipment Loan with the Finance Authority of Maine ("FAME") for a five year term loan, collateralized by all machinery, equipment, furniture, furnishings, fixtures, tools and leasehold improvements located at the Company's Old Town, Maine warehouse and distribution center. The Equipment Loan, consisting of a secured five year term loan in the principal amount of $300,000, bears interest at a fixed per annum rate of 6.0%. Payments of principal and interest in the amount of $5,800 commencing one month from the date entered into and continuing on the same day of each month thereafter until April 4, 2022 (the "Maturity Date"), when, unless sooner paid, the remaining principal and accrued and unpaid interest shall be due and payable in full. The Sterling National Bank Loan Agreement and the Subordinated Loan Agreement were amended in connection with the Equipment Loan to permit the transactions contemplated thereunder. In addition, Sterling National Bank and the Greenwood Parties entered into a separate subordination letter agreement with FAME to permit the repayment of the Equipment Loan and the use of certain equipment as collateral. The proceeds of the FAME loan agreement were used to extinguish the remaining outstanding amount of $73,635 of the FAME loan agreement entered into on November 11, 2013, and other ongoing working capital requirements.

Sale of Equity Securities

On August 18, 2015, the Company completed the sale of 4,000,000 shares of its common stock at a price of $0.50 per share. The sale was made in a private placement offer to its shareholders who are "accredited investors."

The offering was made directly on a best efforts basis without an underwriter or any minimum number of shares that must be sold. The offering commenced on July 28, 2015, and terminated at 5:00 p.m. Eastern Time on August 17, 2015. The shares were issued to accredited investors in private transactions not involving any public offering and exempt from the registration requirements of the Securities Act pursuant to Section 4(a)(2) thereof, and Rule 506(c) of Regulation D thereunder. The offering was open to all shareholders of record as of June 11, 2015, who are accredited investors and currently reside in the United States.

Greenwood Capital, LP, a Massachusetts limited partnership, and MGPLA, L.P., a Delaware limited partnership, both managed by Greenwood Investments, Inc. (the "Greenwood Investors") purchased 3.2 milion.

800,000 shares were also purchased by other eligible stockholders, including the Company's Chairman and CEO, James R. Riedman, who purchased 300,000 shares.

Sterling Loan and Security Agreement

As described in Note 5, "Debt", on February 2, 2015, the Company and Penobscot entered into a Loan and Security Agreement with Sterling National Bank (f/k/a:NewStar Business Credit, LLC), a Delaware limited liability company as administrative agent ("Sterling"), and the lenders party thereto from time to time, and as amended by that certain First Amendment to Loan and Security Agreement dated as of March 18, 2016 (the "Sterling Loan Agreement"), and the Second Amendment to the Loan and Security Agreement dated as of November 3, 2016. The Sterling Loan Agreement provides for up to $9.0 million in borrowing capacity consisting of a revolving line of credit facility of up to $8.0 million (subject to a borrowing base as defined in the Sterling Loan Agreement) with a five-year maturity (the "Sterling Revolving Line of Credit") and a term loan of $1.0 million (the "Term Loan"). Interest on the principal amount outstanding under the Sterling Revolving Line of Credit accrues at a rate equal to the greater of (i) the rate per annum published on each Business Day in the "Money Rates" table of The Wall Street Journal as the one-month LIBOR rate, adjusted daily, and (ii) 1.0% (such greater amount, the "LIBOR Rate") plus 3.75%. Interest on the amount outstanding under the Term Loan accrues at the rate equal to the LIBOR Rate plus 5%. The principal amount of the Term Loan is payable in 36 equal monthly installments of $27,778, together with accrued interest, on the first day of each calendar month beginning March 1, 2015. The obligations of the Company as the borrower under the Sterling Loan Agreement have been guaranteed by Penobscot. As security for the obligations of the Company and Penobscot under the Sterling Loan Agreement, the Company and Penobscot have each granted Sterling (for the benefit of the lenders party to the Sterling Loan Agreement) a security interest in all of their personal property.

Proceeds from the Sterling Loan Agreement were used to pay in full the obligations outstanding under that Loan and Security Agreement dated July 30, 2012 between the Company and AloStar Bank of Commerce, which carried an annual interest rate equal to the LIBOR Rate plus 5.5% and that Loan and Security Agreement dated July 30, 2012 between the Company and Gibraltar Business Capital which carried an annual interest rate of 18.0%.

As a condition to the closing under the Sterling Loan Agreement, the Company also extended from October 30, 2015, until July 31, 2020, the maturity date of the $1,350,000 in aggregate principal amount of its subordinated secured 1% convertible notes held by Greenwood Capital LP.

In the absence of a decline in sales levels, the Company believes that cash flows from operations, the borrowing capacity of Sterling Revolving Line of Credit, and its access to capital will be sufficient to meet the ongoing needs of its business, anticipated growth, flow of inventory, investment requirements and working capital needs for the next twelve months. Additional future financing may be necessary and there can be no assurance that, if needed, the Company will be able to secure additional debt or equity financing with terms acceptable to it or even at all.

Finance Authority of Maine Term Loan

As described in Note 5, “Debt”, on November 11, 2013, the Company entered into an Economic Recovery Program Loan Agreement (the “Equipment Loan”) with the Finance Authority of Maine for a five year term loan, collateralized by all machinery, equipment, furniture, furnishings, fixtures, tools and leasehold improvements located at the Company’s Old Town, Maine warehouse and distribution center. The Equipment Loan, consisting of a secured five year term loan in the principal amount of $200,000, bears interest at a fixed per annum rate of 6.0%.

Sale-Leaseback

Also described in Note 5, “Debt”, on July 1, 2013, the Company completed the sale and contemporaneous leaseback of the land and warehouse (the “Property”) located in Old Town, Maine owned by Penobscot Shoe Company, a wholly-owned subsidiary of the Company (“Penobscot”), to Old Town Partners, LLC (the “Buyer”), pursuant to the terms of a purchase and sale agreement (the “PSA”). Under the PSA, the Company sold the Property to the Buyer for $620,000. Concurrently with the sale, the Company entered into a 10 year commercial lease of the Property with the Buyer.

In the absence of a decline in sales levels, the Company believes that cash flows from operations, the borrowing capacity of its revolving credit facility, and its access to capital will be sufficient to meet the ongoing needs of its business, anticipated growth, flow of inventory, investment requirements and working capital needs for the next twelve months. Additional future financing may be necessary and there can be no assurance that, if needed, the Company will be able to secure additional debt or equity financing with terms acceptable to it or even at all.

3. COMMITMENTS AND CONTINGENCIES

The Company is party to a long-term operating lease for its corporate headquarters in Carlsbad through October 2017, consisting of approximately 5,195 square feet. Minimum lease payments, which take into account escalation clauses, are recognized on a straight-line basis over the minimum lease term. Rent expense included in operations for fiscal 2016 and fiscal 2015 were $99,000 and $83,000, respectively. The increase in rent expense was mostly the result of an increase in the monthly lease payment for both the Carlsbad and China offices beginning in May 2016 and April 2016, respectively.

Future minimum commitments under the facilities and equipment lease agreements are as follows:

Year ending December:		(In thousands)
2017	$	100
2018		24
2019		6
Total	$	130

As described in Note 5, "Debt", on July 1, 2013, the Company entered into a sale and leaseback agreement that was classified as a capital lease. The 10 year initial term of the lease includes a 5 year renewal option. Payments under the lease reduce the lease obligation, and the imputed interest is recorded to interest expense in the Company's consolidated statements of operations. The minimum lease payments under the lease beginning on July 1, 2013, to the end of fiscal 2016 were $118,391.

Future minimum lease payments under the capital lease beginning December 31, 2016 are as follows:

Year ending December:		(In thousands)
2017	$	51
2018		60
2019		69
2020		78
2021		89
Thereafter		155
Total minimum lease payments	$	502

During fiscal year 2016, the Company incurred $75,000 in depreciation expense associated with the amortization of the capital asset.

On April 2, 2013, the Company entered into a three years and nine months licensing agreement with Touchstone Television Productions, LLC ("ABC Studios"), to design, market and distribute footwear for the medical community under the Grey's Anatomy brand. Under the terms of the licensing agreement, the Company is required to pay a royalty fee on net invoiced sales at the end of each quarter over the term of the agreement. The licensing agreement guarantees a minimum royalty payment of $150,000 over its three year term expiring on December 31, 2016. In connection with the licensing agreement, the Company entered into a three year joint marketing agreement with Barco Uniforms, Inc. ("Barco"), an industry leading designer, manufacturer and distributor of uniforms including medical scrubs bearing the Grey's Anatomy label. Under the terms of the joint marketing agreement, the Company has agreed to pay a commission on all sales of its footwear trademarked under the licensing agreement with ABC Studios sold by Barco's sales representatives. Through the end of fiscal 2016, the Company has paid $614,000 in royalties to ABC Studios.

On October 19, 2016, the Company entered into the first amendment of the ABC Studios License Agreement (the "Amended ABC Studios Licensing Agreement") with ABC Studios extending the term for an additional three years expiring on December 31, 2019.

Historically, a majority of the Company's revenue is generated by the sale of women's footwear. Some of these styles have been produced under the ABC Studios License Agreement. Under the ABC Studios License Agreement, the Company has the right to produce, market, and sell footwear under the Grey's Anatomy by Softwalk trademark. The Amended ABC Studios Licensing Agreement guarantees a minimum royalty payment over its three year term expiring on December 31, 2019.

Future minimum royalty payments under this agreement begin on January 1, 2017 and are as follows:

Year ending December:		
2017	$	275
2018	$	275
2019	$	275
Total minimum royalty payments	$	825

The Company, from time to time, may be subject to legal proceedings and claims arising in the normal course of business.

4. DEFINED CONTRIBUTION PLAN

The Company has a defined contribution 401(k) savings plan (the "Plan"), which covers substantially all employees. The Plan allows employees to elect to contribute a portion of their wages on a tax-deferred basis, and the Company may match, at its discretion, a portion of the employee contribution. The company contributed $12,000 and $10,000 during fiscal 2016 and fiscal 2015, respectively.

5. DEBT

Current Loan and Security Agreements

On February 2, 2015, the Company and Penobscot entered into a Loan and Security Agreement with Sterling Business Credit, LLC, a Delaware limited liability company as administrative agent ("Sterling"), and the lenders party thereto from time to time (the "Sterling" Loan Agreement"). The Sterling Loan Agreement provides for up to $9.0 million in borrowing capacity consisting of up to $8.0 million (subject to a borrowing base as defined in the Sterling Loan Agreement) with a five-year maturity (the "RLOC") and a term loan of $1.0 million (the "Term Loan"). The principal amount of the Term Loan is payable in 36 equal monthly installments of $27,778, together with accrued interest, on the first day of each calendar month beginning March 1, 2015. The obligations of the Company as the borrower under the Sterling Loan Agreement have been guaranteed by Penobscot. As security for the obligations of the Company and Penobscot under the Sterling Loan Agreement, the Company and Penobscot have each granted Sterling (for the benefit of the lenders party to the Sterling Loan Agreement) a security interest in all of their personal property. The maturity dates of the RLOC and Term Note are February 2, 2020, and February 2, 2018, respectively.

Interest accrues on the principal amount outstanding under the Revolving Credit Facility at the rate equal to the greater of (i) the rate per annum published on each Business Day in the "Money Rates" table of The Wall Street Journal as the one-month LIBOR rate, adjusted daily, and (ii) 1.0% (such greater amount, the "LIBOR Rate") plus 3.75%. Interest accrues on the principal amount outstanding under the Term Loan at the rate equal to the LIBOR Rate plus 5.0%.

The obligations outstanding under the Revolving Credit Facility and the Term Loan may be prepaid at any time. Beginning with the Company's fiscal year 2016, the Term Loan is subject to a mandatory annual prepayment in an amount equal to the lesser of (i) 25.0% of aggregate excess cash flow (as defined in the Sterling Loan Agreement) of the Company and its subsidiaries for each fiscal year or (ii) $100,000. A prepayment premium will be payable to the lenders if the Company prepays the entire amount outstanding under and terminates the credit facility prior to the third anniversary thereof. The prepayment premium is equal to 3% of the RLOC plus the outstanding principal amount, if any, of the Term Loan in the case of a termination within the first year of the closing, 2% of such sum in the case of a termination within the second year of the closing, and 1% of such sum in the case of a termination within the third year of the closing.

The Sterling Loan Agreement includes various financial and other covenants with which the Company has to comply in order to maintain borrowing availability and avoid penalties, including maintaining minimum tangible net worth and minimum fixed charge coverage ratios.

Other covenants include, but are not limited to, covenants limiting or restricting the Company's ability to incur indebtedness, incur liens, enter into mergers or consolidations, dispose of assets, make investments, pay dividends, enter into transactions with affiliates, or prepay certain indebtedness. The Sterling Loan Agreement also contains customary events of default including, but not limited to, payment defaults, covenant defaults, cross-defaults to other indebtedness, material judgment defaults, inaccuracy of representations and warranties, bankruptcy and insolvency events, defects in Sterling's security interests, change in control events and material adverse change.

At the closing under the Sterling Loan Agreement, the Company used proceeds from the Term Loan and the Revolving Credit Facility to pay in full the obligations outstanding under that Loan and Security Agreement dated July 30, 2012, between the Company, Penobscot and Alostar Bank of Commerce and that Loan and Security Agreement dated July 30, 2012, between the Company and Gibraltar Business Capital and those agreements were terminated.

As a condition to the closing under the Sterling Loan Agreement, the Company also extended from October 30, 2015 until July 31, 2020, the maturity date of the $1,350,000 in aggregate principal amount of its subordinated secured 1% convertible notes held by Greenwood Capital LP and MGPLA LP.

Prior Loan and Security Agreements

On July 30, 2012, the Company and Penobscot entered into a Loan and Security Agreement with AloStar for a three-year revolving credit facility and a three-year term loan, collateralized by substantially all of the assets of the Company and its subsidiaries (as amended, the "AloStar Loan Agreement"). The AloStar Loan Agreement provided for up to $7.25 million in borrowing capacity consisting of a secured first lien revolving credit facility of up to $7.0 million (subject to a borrowing base as defined in the AloStar Loan Agreement) with a three-year maturity (the "AloStar Revolving Credit Facility") and a secured first lien term loan of $250,000 with a three-year maturity (the "AloStar Term Loan").

Concurrently with the execution of the AloStar Loan Agreement, and as a condition thereof, the Company also entered into that certain Subordinated Loan Agreement (as amended, the "Subordinated Loan Agreement") with Gibraltar for a three-year $700,000 term loan collateralized by substantially all of the assets of the Company and its subsidiaries. The Subordinated Loan Agreement provided for up to $700,000 in borrowing capacity consisting of a secured term loan of $700,000, with a maturity of three years and ninety days (the "Gibraltar Term Loan").

As an additional condition to the financing, the Company also concurrently completed the sale of $350,000 of a subordinated secured 1% convertible note (the "2012 Note") to MGPLA, L.P., an affiliate of the Greenwood Purchasers (defined below). The 2012 Note is initially convertible into 1,521,739 shares of the Company's common stock. The sale was made pursuant to a Securities Purchase Agreement dated July 30, 2012 between the Company and the MGPLA, L.P. ("2012 Purchase Agreement"). The 2012 Note has since been assigned to Greenwood Capital LP.

In connection with the issuance of the 2012 Note, the Company also amended and restated certain agreements previously executed and delivered in connection with its sale of the $1.0 million of subordinated secured 1% convertible notes (the "2011 Notes" and collectively with the 2012 Note, the "Greenwood Notes") to Greenwood Investors LP and Greenwood Capital LP (individually, and as the survivor by merger of Greenwood Investors LP with and into Greenwood Capital LP, "Capital") and further, amended the terms of the 2011 Notes to extend the respective maturity dates thereof from July 30, 2014, to October 30, 2015, and provide for the increase in the applicable interest rate pursuant to the terms of the AloStar Loan Agreement that commenced July 30, 2014, on terms consistent with the 2012 Note. As a result of the issuance of the 2012 Note, the conversion rate of the 2011 Notes was automatically adjusted from $0.334 per share to $0.23 per share.

Proceeds from the borrowings made on July 30, 2012, were used to pay in full the outstanding balances of $3.72 million, including $115,000 of prepayment penalties, owed to the Company's prior lenders, Gibraltar and Westran Industrial Loan Co., LLC ("Westran", collectively "Prior Lenders"). As a result, all commitments under the Company's then existing Loan and Security Agreement (the "Prior Loan Agreement") between Gibraltar and Westran, and the related $3,250,000 revolving credit note with Gibraltar, $1,000,000 revolving credit note with Westran, $1,000,000 term loan note with Westran, $500,000 term loan note with Gibraltar, Intellectual Property Security Agreement, and Pledge Agreement each dated November 3, 2010, were terminated, all borrowings thereunder were repaid, and all liens thereunder were released, in each case effective July 30, 2012.

In connection with the AloStar Loan Agreement, the Subordinated Loan Agreement, and the Greenwood Notes, AloStar, Gibraltar, the Greenwood Investors and the Company entered into that certain Intercreditor and Subordination Agreement (as amended, the "Subordination Agreement"), pursuant to which Gibraltar and the Greenwood Investors agreed to subordinate the Company's obligations with respect to the Subordinated Loan Agreement and the Notes to the Company's respective senior debt obligations.

AloStar Loan Agreement:

Borrowings under the AloStar Revolving Credit Facility bore interest at a rate equal to the Daily LIBOR rate, on any day, equal to the greater of (a) 1.0%, and (b) the LIBOR rate as published by the Wall Street Journal on such day for United States dollar deposits for the one month delivery of funds in amounts approximately equal to the principal amount of the loan for which such rate is being determined plus 5.50%. Borrowings under the AloStar Term Loan Facility bore interest at a rate equal to the LIBOR rate plus 7.50%. In addition, the Company was charged a $2,000 monthly loan servicing fee. A prepayment premium was due to the lenders if the Company terminated the credit facility prior to the original three year term date. The prepayment premium was based on 3% of the outstanding credit facility for prepayments within the first year of closing, 2% of the outstanding credit facility for prepayments within the second year of closing, and 1% of the outstanding credit facility for prepayments within the third year of closing prior to the termination date. The AloStar Loan Agreement and related agreements were terminated in connection with the Sterling Loan Agreement entered into on February 2, 2015.

The AloStar Loan Agreement included various financial and other covenants with which the Company had to comply in order to maintain borrowing availability and avoid penalties, including maintaining required EBITDA amounts.

Other covenants included, but were not limited to, covenants limiting or restricting the Company's ability to incur indebtedness, incur liens, enter into mergers or consolidations, dispose of assets, make investments, pay dividends, enter into transactions with affiliates, or prepay certain indebtedness. The AloStar Loan Agreement also contained customary events of default including, but not limited to, payment defaults, covenant defaults, cross-defaults to other indebtedness, material judgment defaults, inaccuracy of representations and warranties, bankruptcy and insolvency events, defects in AloStar's security interests, change in control events and material adverse change. The occurrence of an event of default would have increased the interest rate by 2.0% over the rate otherwise applicable and could have resulted in the acceleration of all obligations of the Company to AloStar with respect to indebtedness, whether under the AloStar Loan Agreement or otherwise.

In connection with the AloStar Loan Agreement, the Company also entered into the following additional agreements with AloStar on July 30, 2012: 1) a Patent Security Agreement and a Trademark Security Agreement in which it granted a continuing security interest in the Company's intellectual property, including its trademarks, goodwill, copyrights, trade secrets, and patents; 2) a Pledge Agreement under which it pledged the shares of its subsidiaries Phoenix Footwear II, Inc., Belt Company, Phoenix Delaware Acquisition, Inc. Penobscot and PXG Canada, Inc., as collateral for the loans; and 3) a Deposit Account Control Agreement with Pacific Western Bank, with respect to the security interest granted AloStar in the Company's deposit account with Pacific Western Bank.

Gibraltar Subordinated Loan Agreement:

Borrowings under Gibraltar's Term Loan Facility bore interest at a rate equal to the prime rate, with a floor of 3.25%, plus 14.75%. Interest only payments were due monthly until July 1, 2013, at which point monthly interest payments will continue while the principal balance will paid in quarterly installments of $30,000, with a balloon payment due at maturity. A prepayment premium of $28,000 was due to the lenders if the Company terminated the credit facility prior to the original three year term date. The Gibraltar Subordinated Term Loan Agreement was terminated and paid off in connection with the Company's entering into the Sterling Loan Agreement on February 2, 2015.

The Subordinated Loan Agreement included various financial and other covenants with which the Company had to comply in order to maintain borrowing availability and avoid penalties, including maintaining required EBITDA amounts.

Other covenants included, but were not limited to, covenants limiting or restricting the Company's ability to incur indebtedness, incur liens, enter into mergers or consolidations, dispose of assets, make investments, pay dividends, enter into transactions with affiliates, or prepay certain indebtedness. The Subordinated Loan Agreement also contained customary events of default including, but not limited to, payment defaults, covenant defaults, cross-defaults to other indebtedness, material judgment defaults, inaccuracy of representations and warranties, bankruptcy and insolvency events, defects in Gibraltar's security interests, change in control events and material adverse change. The occurrence of an event of default would have increased the interest rate by 4.0% over the rate otherwise applicable and could have resulted in the acceleration of all obligations of the Company to Gibraltar with respect to indebtedness, whether under the Subordinated Loan Agreement or otherwise.

In connection with the Subordinated Loan Agreement, the Company also entered into the following additional agreements with Gibraltar on July 30, 2012, in each case subject to the terms of the Subordination Agreement: 1) an Intellectual Property Security Agreement in which it granted a continuing security interest in the Company's intellectual property, including its trademarks, goodwill, copyrights, trade secrets, and patents; and 2) a Pledge Agreement under which it pledged the shares of its subsidiaries Phoenix Footwear II, Inc., Belt Company, Phoenix Delaware Acquisition, Inc. Penobscot and PXG Canada, Inc., as collateral for the loans.

2012 Purchase Agreement:

Convertible Subordinated Secured Notes

On July 21, 2011, the Company completed the sale of the 2011 Notes to the Greenwood Purchasers. Capital is an affiliate of and managed by General Partner, its sole general partner. Steven Tannenbaum is the President of General Partner (the Greenwood Investors, General Partner and Mr. Tannenbaum are referred to collectedly herein as the "Greenwood Parties"). The 2011 Notes were initially convertible into 2,994,011 shares of the Company's common stock. The 2011 Notes were initially due on October 30, 2015. As a condition to the closing under the Sterling Loan Agreement, the Company extended the maturity date from October 30, 2015, until July 31, 2020. The 2011 Notes bear interest at the rate of 1.0% per annum. The interest is payable in cash semiannually in arrears on October 31, and April 30 of each year, commencing October 31, 2011. No prepayment may be made by the Company without Greenwood Purchasers' consent. Capital may convert all or part of the 2011 Notes into common stock of the Company until the maturity date. As a result of the Company's issuance of the 2012 Note, the conversion price of the 2011 Notes was reduced to $0.23, at which price the 2011 Notes are convertible into 4,347,826 shares of the Company's common stock. The conversion price remains subject to adjustment in the event of certain corporate transactions, including but not limited to, certain issuances of common stock at a price below the conversion price of the 2011 Notes. The 2011 Notes also provide for mandatory conversion into common stock in the event certain market conditions are met for the trading of the Company's stock, including a trading price of at least $1.00 per share on each trading day during any period of 90 consecutive days ended within 10 days prior to determination, or in the event a change in control results from the sale of the Company in a merger, stock or asset sale for a cash price of at least $5.00 per share.

The 2011 Notes contain customary events of default including, but not limited to, payment defaults, failure to deliver shares on conversion, cross-defaults to other agreements in the transaction, cross defaults to other indebtedness of $50,000 or more in the aggregate, material judgment defaults, inaccuracy of representations and warranties, bankruptcy and insolvency events, and other occurrences including change in control. The occurrence of an event of default will increase the interest rate to 13.0% and could result in the acceleration of all obligations of the Company to Capital with respect to the 2011 Notes.

The obligation under the 2011 Notes is secured by a pledge of substantially all of the Company's assets, including its intellectual property and stock of its Penobscot. The security is provided under the Security Agreement, Intellectual Property Security Agreement and Pledge Agreement between the Company, the Greenwood Investors and Greenwood Investments, Inc., as agent for the Greenwood Investors, each of which were amended and restated as discussed herein.

As required under the terms of the transaction, the Board of Directors approved the Amended and Restated By-Laws of the Company to i) eliminate the restriction on stockholders ability to act by written consent in lieu of a meeting with less than unanimous consent; ii) permit holders of at least 15% of the outstanding stock eligible to vote at a meeting to call a special meeting of stockholders; and iii) to incorporate the reduction of the size of the board from 7 to 4. In addition, the Company entered into (1) an Amendment of the Employment Agreement with James Riedman, the Company's Chief Executive Officer to eliminate its automatic renewal so it will terminate by its terms on December 31, 2012, and to provide that no severance will be paid if the agreement expires by virtue of it reaching the end of its term, and (2) an indemnification agreement with Stephanie Pianka, as a director of the Company.

Other agreements entered into in connection with the transaction with the Greenwood Purchasers, which have each been subsequently replaced or amended and restated as set forth above, included: (1) a Subordination and Intercreditor Agreement, subordinating the security interest of the Greenwood Purchasers to the rights of the Prior Lenders, together with a related Waiver and Consent provided by the Prior Lenders to the Company with respect to certain provisions under its credit facility and related loan agreements, to permit the issuance of the 2011 Notes to the Greenwood Purchasers; (2) the Investors Agreement; and (3) the Voting Agreement.

2012 Convertible Note.

Since its original issuance, the 2012 Note has been assigned from MGPLA, L.P. to Greenwood Capital LP.

The 2012 Note was initially due October 30, 2015, and bore interest at the initial rate of 1.0% per year. As a condition of the closing under the Sterling Loan Agreement, the Company extended the maturity date from October 30, 2015 until July 31, 2020. The interest is payable in cash semi-annually in arrears on October 31 and April 30 of each year, commencing October 31, 2012, and the rate increases to the applicable interest rate under the Loan Agreement commencing July 30, 2014. No prepayment may be made by the Company without Greenwood Capital, LP's consent. Greenwood Capital LP may convert all or part of the 2012 Note into common stock of the Company at a conversion price equal to $0.23 until the maturity date. The initial conversion price is subject to adjustment in the event of certain corporate transactions, including but not limited to, certain issuances of common stock at a price below the conversion price of the 2012 Note. The 2012 Note also provides for mandatory conversion into common stock in the event certain market conditions are met for the trading of the Company's stock, including a trading price of at least $1.00 per share on each trading day during any period of 90 consecutive days ending within 10 days prior to the date of determination, or in the event a change of control results from a sale of the Company in a merger, stock or asset sale for a cash price of at least $5.00 per share.

The maturity date of the Greenwood Notes was extended to July 31, 2020, in connection with the Company entering into the Sterling Loan Agreement on February 2, 2015.

The 2012 Note contains customary events of default including, but not limited to, payment defaults, failure to deliver shares on conversion, cross-defaults to other agreements in the transaction, cross-defaults to other indebtedness of $50,000 or more in the aggregate, material judgment defaults, inaccuracy of representations and warranties, bankruptcy and insolvency events, defects in the security interests, unresolved judgments of $50,000 or more in excess of insurance coverage and change in control events. The occurrence of an event of default will increase the interest rate to 13.0% and could result in the acceleration of all obligations of the Company to Greenwood Capital, LP with respect to indebtedness.

In addition to the sale of the 2012 Note, the 2012 Purchase Agreement also required that the parties amend and restate the following additional agreements, subject to the Subordination Agreement, to include MGPLA, L.P. as a party:

Security Agreement, IP Security Agreement, Pledge Agreement. The obligation under the Notes is secured by a pledge of substantially all of the Company's assets, including its intellectual property assets and the stock of its wholly-owned subsidiary, Penobscot. The security interest is provided under the Security Agreement, Intellectual Property Security Agreement and Pledge Agreement between the Company, the Greenwood Investors and Greenwood Investments, Inc., as agent for the Greenwood Investors, each dated July 30, 2012.

Subordination Agreement. The security interest of the Greenwood Investors was subordinated to the rights of AloStar and Gibraltar under their respective $7.25 million credit facility and $700,000 term note, pursuant to the terms and conditions of the Subordination Agreement.

Investors Agreement:

Registration Rights. Under the Investors Agreement between the Company, the Greenwood Investors, James Riedman, and Riedman Corporation dated July 30, 2012, and as amended on July 23, 2015 (the "Investors Agreement"), the Greenwood Investors received registration rights under which they may make a demand for registration of the shares underlying the Notes and other shares held by the Greenwood Investors and their affiliates. The demand may not be made until after the earlier of 3 years after July 21, 2011, or 180 days after the effective date of an initial public offering registration statement. The Company must thereafter file a registration statement within 60 days of a demand. The Greenwood Investors are limited to two demands for a Registration Statement on Form S-1. If the Company is eligible to use Form S-3, it must file a registration statement within 45 days of a demand and there is no limit on the number of such demands. The Greenwood Investors also obtained unlimited piggyback registration rights. Each of the categories of registration rights are subject to an underwriter's cutback. The agreement also obligates the Company make current information available to the public to meet the requirements of Rule 144.

Matters Requiring Investor Approval. Under the Investors Agreement, the Company may not take certain actions without the approval of Greenwood Investments, Inc., including but not limited to: increase or decrease its authorized capital stock, or authorize new classes or series of capital stock or securities convertible into common stock; amend its certificate of incorporation or by-laws; enter into a merger or sell all or substantially all of the properties or assets of the Company and its subsidiaries; dissolve; declare or pay any dividend; issue or obligate itself to issue any security, other than shares of common stock, except upon certain outstanding obligations; redeem any shares; increase or decrease the authorized size of the Board of Directors, except as expressly contemplated by the Voting Agreement; acquire all or any portion of any business or product line; enter into any material joint ventures, strategic alliances, or major partnerships; incur of any indebtedness outside the ordinary course of business other than under the agreements executed concurrently therewith; hire, terminate, or increase the compensation of James R. Riedman and any other person holding the position of chief executive of the Company; approve or authorize any transaction or series of related transactions outside the ordinary course of business involving $250,000 or more.

Matters Requiring Board Approval. Under the Investors Agreement, management may not take the following actions without approval of the board of directors, including but not limited to: materially modify any existing loans; approve or authorize any material modification to or material deviation from the Company's budget; increase the compensation of any director; approve the settlement by the Company of any material litigation or other proceedings relating to the Company; pay any capital expenditures in excess of $100,000 during any 12-month period other than a specific identifiable line item previously approved in the budget.

Standstill. Under the Investors Agreement, the Greenwood Investors and James R. Riedman and Riedman Corporation (the "Riedman Shareholders") each agreed to a standstill whereby they will not acquire any common stock or other securities of the Company in an open-market transaction unless approved in advance to do so by the Company's board of directors, and (i) in the case of the Riedman Shareholders, unless approved by Greenwood Investments, Inc. ("General Partner"), or (ii) in the case of the Greenwood Investors or any of their affiliates, by a director not appointed by or affiliated in any way with the Investors). The Riedman Shareholders are parties to the Investors Agreement solely for purposes of this standstill provision.

Participation Rights. The Greenwood Investors also obtained participation rights so that they shall be entitled to a right to purchase, on a pro rata basis, all or any part of any new securities issued by the Company, with certain exceptions for preexisting obligations by the Company to issue other securities.

Voting Agreement. The Company, the Greenwood Investors and the Riedman Shareholders also amended and restated that certain Voting Agreement dated July 21, 2011, and as amended on July 23, 2015 (the "Voting Agreement"), as part of the transaction. The Riedman Shareholders agreed to elect one designee of the Investors as a member of the board of directors. The Investors agreed to elect one designee of the Riedman Shareholders to the Board. The parties also agreed to vote as necessary to ensure that the size of the board of directors shall be set and remain at four directors until the directors are next elected by stockholders, or at such earlier time as may be requested by the Greenwood Investors upon their written request, on which date the size of the board shall be reduced and set and remain at three directors.

Capital Lease Obligation

On July 1, 2013, the Company completed the sale and contemporaneous leaseback of the Property to the Buyer, pursuant to the terms of the PSA. Under the PSA, the Company sold the Property to the Buyer for $620,000. Concurrently with the sale, the Company entered into a 10 year commercial lease of the Property with the Buyer. In addition, the AloStar Loan Agreement and the Subordinated Loan Agreement were amended to permit the consummation of the transactions completed by the PSA. The proceeds of the transaction were used to pay off the balance of its $250,000 term loan with AloStar, and pay down its $700,000 subordinated term note with Gibraltar, and its $7.0 million revolving credit facility with AloStar.

The sale and leaseback transaction of the Property was classified as a capital lease as the present value of the minimum future lease payments using the Company's incremental borrowing rate, exceeded the selling price of the Property. As a result, the Company recorded a capital leased asset and corresponding capital leased obligation at a fair value of $620,000, equal to the selling price of the Property. The $224,000 gain on the sale of the Property was deferred and will be recognized in proportion to depreciation of the capital leased asset over the ten (10) year initial term of the lease. Payments under the lease agreement reduce the lease obligation, and the imputed interest is recorded to interest expense in the Company's consolidated statements of operations.

Finance Authority of Maine Term Loan

On November 11, 2013, the Company entered into an Equipment Loan with the Finance Authority of Maine ("FAME") for a five year term loan, collateralized by all machinery, equipment, furniture, furnishings, fixtures, tools and leasehold improvements located at the Company's Old Town, Maine warehouse and distribution center. The Equipment Loan, consisting of a secured five year term loan in the principal amount of $200,000, bears interest at a fixed per annum rate of 6.0%. Payments of principal and interest in the amount of $3,867 commencing one month from the date entered into and continuing on the same day of each month thereafter (except for any month not containing such a day, in which case it shall be due the last day of that month) until November 11, 2018 (the "Maturity Date"), when, unless sooner paid, the remaining principal and accrued and unpaid interest shall be due and payable in full. The AloStar Loan Agreement and the Subordinated Loan Agreement were amended in connection with the Equipment Loan to permit the transactions contemplated thereunder. In addition, AloStar, Gibraltar, and the Greenwood Parties entered into a separate subordination letter agreement with FAME to permit the repayment of the Equipment Loan and the use of certain equipment as collateral.

IBM Capital Lease Agreement

On November 26, 2014, the Company entered into a two year capital lease agreement with IBM Credit LLC to purchase computer server hardware and software in the principal amount of $64,311 bearing an imputed per annum interest rate of 6.0% with 24 periodic payments in the amount of $2,744 due through November 2016. The server hardware and software was placed into services during the first quarter of fiscal 2015.

As of December 31, 2016 and January 2, 2016, debt consisted of the following:

	December 31, 2016	January 2, 2016
	(In thousands)	
Term loan facility with Finance Authority of Maine; secured by the Company's personal property in the Maine warehouse and distribution center; interest payable monthly at a rate of 6% annum…………………………………………………………………………..	$ 84	$ 124
Revolving line of credit with Sterling National Bank; secured by all of the Company's personal property; interest payable monthly and bears a rate equal to the greater of 1% or the Daily LIBOR rate plus 5.0% per annum (stated rate of 4.75% at December 31, 2016)	4,424	5,156
Subordinated secured 1% convertible notes with Greenwood Capital LP; secured by all of the Company's personal property; interest payable semi-annually on October 31st and April 30th at a rate of 1% per annum until July 29, 2014, after which the rate increased to the applicable interest rate under the AloStar Loan Agreement…………………………………	1,000	1,000
Subordinated secured 1% convertible note with Greenwood Capital LP; secured by all of the Company's personal property; interest payable semi-annually on October 31st and April 30th at a rate of 1% per annum until July 30, 2014, after which the rate increased to the applicable interest rate under the AloStar Loan Agreement…………………………………………………..	350	350
Capitalized leased obligation: 10 year capital lease with Old Town Partners, LLC terminating on June 30, 2023. Lease payments are allocated to the reduction of the capital lease obligation and the interest expense with an imputed per annum rate of 9.5%	502	544
Capitalized leased obligation: 2 year capital lease with IBM Corporation maturing on December 26, 2016. Lease payments are allocated to the reduction of the capital lease obligation and the interest expense with an imputed per annum rate of 6.0%..........................	—	30
Term loan facility: 3 year term note with Sterling National Bank maturing on February 2, 2018, secured by all of the Company's personal property; principal of $27,778 is paid monthly and bears interest at a rate equal to the greater of 1% or thee Daily LIBOR rate plus 5.0% per annum (stated rate of 6.0% at December 31,2016) …………………………………	389	694
	$ 6,749	$ 7,898
Current portion of long term debt	4,851	5,602
Long term debt, net of current portion	$ 1,898	$ 2,296

The Sterling Loan Agreement and the Subordinated Loan Agreement include various financial and other covenants, with which the Company had to comply in order to maintain borrowing availability and avoid penalties including maintaining required monthly minimum Tangible Net Worth and Fixed Coverage Ratio.

As of December 31, 2016, the Company was not in compliance with the Fixed Charge Coverage Ratio ("FCCR") of 1.15:1.00 and the minimum Tangible Net Worth covenant of $3.1 million of the Loan and Security Agreement with its Lender. On April 21, 2017, Sterling National Bank and the Company entered into the Second Amendment of the Loan and Security Agreement waving the FCCR and Minimum Tangible Net Worth covenants as of December 31, 2016 and through April 1, 2017, resetting the minimum Tangle Net Worth covenant and replacing the FCCR covenant with a minimum Free Cash Flow covenant beginning in April 2017 reporting period through the November 2017 reporting period, and then reverting back to a minimum FCCR thereafter.

As of December 31, 2016, the Company had $1.0 million in available borrowing capacity under its Revolving Credit Facility with Sterling Business Credit.

The Company incurred $261,000 in prepaid debt issuance costs in connection with the Sterling Loan Agreement. The prepaid debt issuance cost includes legal, appraisal and other loan document fees in addition to a commitment fee of $112,500. Capitalized debt issuance fees are amortized into expense over the loan term and totaled $57,000 in 2016 and $130,000 in 2015. Debt issuance costs incurred during 2016 were primarily related to the amortization of prepaid debt costs associated with the Sterling Loan Agreement as well as the term loan with the Financial Authority of Maine. Debt issuances costs during 2015 were the result of the acceleration of expense associated with the termination of the AloStar Loan Agreement and the Gibraltar Business Capital Loan Agreement, debt issuance costs associated with the Sterling Loan Agreement and amortization of debt costs resulting from the term loan with the Financial Authority of Maine.

6. STOCK-BASED COMPENSATION

On July 1, 2011, the Board of Directors adopted and approved the 2011 Long-Term Incentive Plan of Phoenix Footwear Group, Inc. (the "2011 Plan"), subject to stockholder approval which was obtained on June 29, 2012, to renew the Amended and Restated 2001 Long-Term Incentive Plan of the Company which had expired by its terms. Under the 2011 Plan the Company may grant stock options, stock appreciation rights, stock awards and other awards from time to time to key employees, officers, directors, advisors and independent consultants to the Company or to any of its subsidiaries. Shares available for future option and restricted stock grants totaled 897,204 as of December 31, 2016.

Total stock-based compensation expense recognized for fiscal 2016 and fiscal 2015 were as follows:

	Twelve Months ended	
	December 31, 2016	January 2, 2016
	(In thousands)	
Selling, general and administrative	$ 34	$ 108
Pre-tax stock-based compensation expense	34	108
Total stock-based compensation expense	$ 34	$ 108

Options

In general, options become exercisable over either a two or three-year period from the grant date and expire 10 years after the date of grant. The fair value of each option award is estimated on the date of the grant using the Black-Scholes-Merton option pricing model. Expected volatilities are based on historical volatility of the Company's stock price and implied. The Company uses historical data to estimate an option's expected life; the expected life for grants to senior management-level employees and other employees are considered separately for valuation purposes. The risk-free interest rate input is based on the U.S. Treasury yield curve in effect at the time of the grant. Compensation cost, net of projected forfeitures, is recognized on a straight-line basis over the period between the grant and vesting dates, with compensation cost for grants with a graded vesting schedule recognized on a straight-line basis over the requisite service period for each separately vesting portion of the award as if the award was, in substance, multiple awards. During fiscal 2016 and fiscal 2015 the Company granted zero option awards.

The aggregate intrinsic value of options exercised during fiscal 2016 and fiscal 2015 was zero. The unrecognized compensation cost related to stock option awards at December 31, 2016, was zero.

The following table summarizes the stock option transactions during fiscal 2016 and fiscal 2015:

	Options	Weighted Average Exercise Price	Aggregate Intrinsic Value
	(In thousands, except exercise price)		
Options outstanding , January 3, 2015	1,040	$ 6.54	—
Options granted	—	—	
Options exercised	—	—	
Options cancelled	(30)	$ 5.84	
Options outstanding, January 2, 2016	1,010	$ 0.28	$ 88
Options granted	—	—	
Options exercised	—	—	
Options cancelled	—	$ —	
Options outstanding, December 31, 2016	1,010	$ 0.28	$ 70
Options exercisable, December 31, 2016	1,010	$ 0.28	$ 70

The following table summarizes information about employee stock options outstanding and exercisable at December 31, 2016.

	Options Outstanding			Options Exercisable	
Range of Exercise Price	Number Outstanding at December 31, 2016	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable at December 31, 2016	Weighted Average Exercise Price
	(In thousands, except years and exercise price)				
$0.23 to $0.28	960	6.2 years	$ 0.24	960	$ 0.24
$1.00	50	4.3 years	$ 1.00	50	$ 1.00
Total	1,010	6.1 years	$ 0.28	1,010	$ 0.28

Restricted Stock Rights

In general, service-based stock rights vest over a two-year period from the grant date. Performance-based stock rights cliff vest based on specifically defined performance criteria consisting primarily of revenue, income and shareholder value targets and expire generally within a three to five-year period if the performance or service criteria have not been met. The Company deems stock rights to be equivalent to a stock option for the purpose of calculating dilutive shares.

Compensation cost for restricted stock rights is measured as the excess, if any, of the quoted market price of the Company’s stock at the grant date over the amount the holder must pay to acquire the stock (which is generally zero). Compensation cost, net of projected forfeitures, is recognized over the period between the issue date and the date any restrictions lapse, with compensation cost for grants with a graded vesting schedule (service-based) recognized on a straight-line basis over the requisite service period for the total award. In any event, compensation expense is not recognized, if at all, until vesting is considered probable.

On April 1, 2016, the Company granted to each of its non-employee directors 20,000 service based restricted shares of common stock contingent upon the directors continued membership on the Company's Board through March 31, 2017.

As of December 31, 2016, the total compensation cost related to stock-based awards granted to non-employee directors but not yet recognized was $6,200.

The following table summarizes service-based and performance-based stock rights issued as of December 31, 2016:

	Stock Rights
	(In thousands)
Stock Rights outstanding January 3, 2015	60
Granted	60
Cancelled	—
Exercised	(60)
Stock Rights outstanding January 2, 2016	60
Granted	90
Cancelled	—
Exercised	(70)
Stock Rights outstanding December 31, 2016	80

In addition to the stock options and restricted stock rights outstanding under the 2011 Plan, the Company granted options to one separate major stockholders in consideration for debt and debt guarantees. Options outstanding and exercisable under these arrangements totaled 50,000 as of December 31, 2016. These options were granted July 17, 1997 with an exercise price of $2.38 per share.

7. INCOME TAXES

The Company uses the asset and liability method of accounting for income taxes, in accordance with ASC 740-10 (formerly SFAS 109), which requires that the Company recognize deferred tax liabilities for taxable temporary differences and deferred tax assets for deductible temporary differences and operating loss carry-forwards using enacted tax rates in effect in the years the differences are expected to reverse. Deferred income tax benefit or expense is recognized as a result of changes in net deferred tax assets or deferred tax liabilities. A valuation allowance is recorded when it is more likely than not that some or all of any deferred tax assets will not be realized. As of December 31, 2016 and January 2, 2016, the Company had a full valuation allowance on its deferred tax assets.

The following summarizes the income tax expense (benefit) for fiscal 2016 and fiscal 2015:

	2016	2015
	(In thousands)	
Current:		
Federal	$ —	$ 8
State	4	1
Foreign	—	—
	4	9
Deferred:		
Federal	—	—
State	(29)	(9)
	(29)	(9)

	2016	2015
	(In thousands)	
Income tax expense (benefit)	$ (25)	$ —

Current income taxes (benefits) are based upon the year's income taxable for federal, state and foreign tax reporting purposes. Deferred income taxes (benefits) are provided for certain income and expenses, which are recognized in different periods for tax and financial reporting purposes.

Deferred tax assets and liabilities are computed for differences between the financial statements and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the period in which the differences are expected to affect taxable income.

The Company's policy is not to record deferred income taxes on the undistributed earnings of foreign subsidiaries that are indefinitely reinvested in foreign operations.

A reconciliation of the expected tax computed at the U.S. statutory federal income tax rate to the total benefit for income taxes at December 31, 2016 follows:

	2016	2015
	(In thousands)	
Benefit for federal income taxes at the statutory rate	(421)	$ (351)
State and other taxes, net of federal benefit	(13)	(6)
Items not deductible	10	15
Decrease of the valuation allowances	429	348
Decrease in the FIN48 liability	(30)	(9)
Other, net	—	3
Income tax expense (benefit)	$ (25)	$ —

Significant components of the Company's deferred tax assets (liabilities) as of December 31, 2016 and January 2, 2016 are as follows:

	2016		2015	
	Current	Non-current	Current	Non-current
	(In thousands)		(In thousands)	
ASSETS				
Non-deductible allowances for doubtful accounts	$ 76	$ —	$ 15	$ —
UNICAP	92	—	110	—
Earn-out	—	—	—	—
Other accruals	866	37	868	54
Capital loss carryforward	—	—	—	—
Net operating loss carryforwards	—	13,094	—	13,348
Depreciation		85		83
Credits	—	15	—	15
LIABILITIES				
Depreciation	—	—	—	—
Deferred income tax asset (liability)	1,034	13,231	993	13,500
Valuation allowances	(1,034)	(13,231)	(993)	(13,500)
Net deferred tax asset (liability)	$ —	$ —	$ —	$ —

In assessing the realizability of deferred tax asset of $14.3 million at December 31, 2016, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. The Company has determined it is more likely than not that its deferred tax assets will not be realized. Accordingly, a valuation allowance has been recorded at December 31, 2016, to fully offset the deferred tax asset of $14.3 million.

As of December 31, 2016, the Company had approximately $36.0 million of net operating loss carryforwards available for federal tax purposes which begin to expire in 2028. As of December 31, 2016, the Company also had approximately $11.0 million of net operating loss carryforwards for California and $6.0 million of net operating losses for other states. These net operating losses begin to expire in 2016.

Utilization of the NOL carryforwards may be subject to a substantial annual limitation due to ownership change limitations that may have occurred or that could occur in the future, as required by Section 382 of the Internal Revenue Code of 1986, as amended (the “Code”), as well as similar state and foreign provisions. These ownership changes may limit the amount of NOL and R&D credit carryforwards that can be utilized annually to offset future taxable income and tax, respectively. In general, an “ownership change” as defined by Section 382 of the Code results from a transaction or series of transactions over a three-year period resulting in an ownership change of more than 50 percentage points of the outstanding stock of a company by certain shareholders.

The Company has not completed a study to assess whether an ownership change has occurred or whether there have been multiple ownership changes since the Company’s formation due to the complexity and cost associated with such a study, and the fact that there may be additional such ownership changes in the future.

On December 31, 2016, the Company complied with Accounting for Uncertain Tax positions pursuant to ASC 740. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (excluding interest and penalties):

		(In thousands)
Unrecognized tax benefits, January 2 , 2016	$	16
Increases for prior year tax positions		None
Decreases for prior year tax positions		None
Increases for current year tax positions		None
Settlements		None
Administrative practice relief		(16)
Unrecognized tax benefits, December 31, 2016	$	—

Included in the balance of unrecognized tax benefits at December 31, 2016, are approximately $30,000 of tax benefits that, if recognized, would affect the effective tax rate (including interest and penalties).

It is not anticipated that there will not be a significant change in unrecognized tax benefits over the next twelve months.

The Company recognizes interest and penalties related to unrecognized tax benefits in income tax expense. As of December 31, 2016, the Company had approximately $14,000 of accrued interest and penalties related to uncertain tax positions.

The Company is subject to taxation in the U.S. and various state tax jurisdictions. As of December 31, 2016 the Company is no longer subject to federal examinations for the year before 2012; and for California and Canadian examinations before 2011. Generally the tax years remain open for examination by the tax authorities under a four year statute of limitations; however, certain states may keep their statute open for six to ten years.

8. SUBSEQUENT EVENTS

On April 4, 2017, the Company entered into an Equipment Loan with the Finance Authority of Maine (“FAME”) for a five year term loan, collateralized by all machinery, equipment, furniture, furnishings, fixtures, tools and leasehold improvements located at the Company’s Old Town, Maine warehouse and distribution center. The Equipment Loan, consisting of a secured five year term loan in the principal amount of $300,000, bears interest at a fixed per annum rate of 6.0%. Payments of principal and interest in the amount of $5,800 commencing one month from the date entered into and continuing on the same day of each month thereafter until April 4, 2022 (the "Maturity Date"), when, unless sooner paid, the remaining principal and accrued and unpaid interest shall be due and payable in full. The Sterling National Bank Loan Agreement and the Subordinated Loan Agreement were amended in connection with the Equipment Loan to permit the transactions contemplated thereunder. In addition, Sterling National Bank and the Greenwood Parties entered into a separate subordination letter agreement with FAME to permit the repayment of the Equipment Loan and the use of certain equipment as collateral. The proceeds of the FAME loan agreement were used to extinguish the remaining outstanding amount of $73,635 of the FAME loan agreement entered into on November 11, 2013, and will be used for other ongoing working capital requirements.

On March 31, 2017, the Company issued an aggregate of 80,000 shares of restricted common stock to four non-employee directors, Steven DePerrior, Stephanie Pianka, Frederick Port, and David Whalen in transactions exempt from registration pursuant to Rule 701 under the Securities Act, pursuant to awards granted under the 2011 Long-Term Incentive Plan of Phoenix Footwear Group, Inc. (the "2011 Plan"), upon the satisfaction of vesting criteria which required that the recipients maintain continued membership on the Company's Board of Directors through March 31, 2017. The shares are restricted from transfer unless in compliance with applicable securities laws and the certificates representing the shares contain a customary restrictive legend.

The company has evaluated subsequent events through April 25, 2017, which is the date the consolidated financial statements were available to be issued.

.SCHEDULE II CONSOLIDATED VALUATION AND QUALIFYING ACCOUNTS
For The Years Ended December 31, 2016 and January 2, 2016

	Sales and Sales Returns Allowances and Allowance for Doubtful Accounts	Reserve for Obsolete Inventory
	(In thousands)	
Balance, January 3, 2015	$ 1,108	$ 300
Provision	4,932	414
Write-off, disposal, costs, and other	(4,759)	(221)
Balance, January 2, 2016	$ 1,281	$ 493
Provision	5,503	445
Write-off, disposal, costs, and other	(5,291)	(521)
Balance, December 31, 2016	$ 1,493	$ 417

EXHIBIT B

Management's Discussion and Analysis ("MD&A") of Financial Condition and Results of Operations

The following discussion provides information and analysis of the Company's results of operations and its liquidity and capital resources, and should be read in conjunction with the Company's Consolidated Financial Statements and the other financial information included in Exhibit A and elsewhere in this Annual Report. This discussion contains forward-looking statements that involve risks and uncertainties. The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of any number of factors.

The Company's operating and reporting period is on a 52-53 week fiscal year ending on the Saturday nearest to December 31. The Company refers to the fiscal year ended January 3, 2015 as "fiscal 2014," the fiscal year ending January 2, 2016 as "fiscal 2015," and the fiscal year ending December 31, 2016 as "fiscal 2016." The 52-week fiscal years consist of four equal quarters of 13 weeks each, and the 53-week fiscal years consist of three 13-week fiscal quarters and one 14-week fiscal quarter. The financial results for the 53-week fiscal years and 14-week fiscal quarters will not be exactly comparable to the 52-week fiscal years and 13-week fiscal quarters. Fiscal 2015 and fiscal 2016 each include 52 weeks and fiscal 2014 includes 53 weeks.

General

Phoenix Footwear Group, Inc. specializes in quality comfort women's and men's footwear. The Company designs, develops, markets, and sells footwear in a wide range of sizes and widths under the brands Trotters®, SoftWalk®, and beginning in April of fiscal 2013, Grey's Anatomy by SoftWalk®. The Company has been engaged in the manufacture or importation and sale of quality footwear since 1882.

Trotters and SoftWalk products are sold by the Company's own dedicated employee sales force that covers the U.S. market. Beginning with fiscal 2011, the Company distributes its products in Canada under an exclusive distribution agreement with an independent third party, Canada Shoe Corp, the sole importer and distributor of the Company's Trotters and SoftWalk brands in Canada. Prior to fiscal 2011, the Company sold Trotters and SoftWalk products in Canada through its wholly-owned Canadian subsidiary, which utilized independent sales representatives.

On April 2, 2013, the Company entered into a three year licensing agreement with Touchstone Television Productions, LLC ("ABC Studios"), to design, market and distribute footwear for the medical community under the Grey's Anatomy brand. Concurrent with the ABC Studios licensing agreement, the Company entered into a three year joint marketing agreement with Barco Uniforms, Inc. ("Barco"), an industry leading designer, manufacturer and distributor of uniforms, including medical scrubs bearing the Grey's Anatomy label. Under the terms of the joint marketing agreement, the Company has agreed to pay a commission on all sales of its footwear trademarked under the licensing agreement with ABC Studios sold by Barco's sales representatives.

On October 19, 2016, the Company entered into the first amendment of the ABC Studios License Agreement (the "Amended ABC Studios Licensing Agreement") with ABC Studios extending the term for an additional three years expiring on December 31, 2019.

During fiscal 2016, the Company's products were carried by approximately 835 customers in over 1,405 retail locations throughout the United States. The Company's distribution channels include department stores, leading specialty and independent retail stores, mail order catalogues, internet retailers and independent uniform suppliers. The Company also operates its own direct to consumer internet retail business.

Fiscal 2016 Financial Overview

Continuing Operations. Net sales from operations for fiscal 2016 were $20.2 million, a decrease of $1.4 million or 6.5%, compared to net sales of $21.7 million for fiscal 2015. The loss from operations was $1.2 million, an increase in net loss of $189,000 or 18.3%, compared to a net loss from operations of $1.0 million during fiscal 2015.

The Company's working capital as of December 31, 2016 and January 2, 2016 was $3.0 million and $4.5 million, respectively.

Net Loss/Earnings Per Share. Net loss per share from operations for fiscal 2016 was $0.10 compared to a net loss per share of $0.11 from operations for year 2015.

Results of Operations

Fiscal 2016 Compared to Fiscal 2015

The following table sets forth selected consolidated operating results stated in dollars and as a percentage of net sales:

	12 Months Ended					
	December 31, 2016		January 2, 2016		Increase (Decrease)	
			(In thousands)			
Net sales	$ 20,244	100%	$ 21,655	100%	$ (1,411)	(7)%
Cost of goods sold	12,817	63%	14,374	66%	(1,557)	(11)%
Gross profit	7,427	37%	7,281	34%	146	2%
Operating expenses:						
Selling, general and administrative	8,058	40%	7,537	35%	521	7%
Total operating expenses	8,058	40%	7,537	35%	521	7%
Operating loss	(631)	(3)%	(256)	(1)%	(375)	*%
Interest expense, net	590	3%	776	4%	186	(24)%
Loss before income taxes	(1,221)	(6)%	(1,032)	(5)%	(189)	(18)%
Income tax expense (benefit)	(25)	— %	—	— %	25	*%
Net Loss	$ (1,196)	(6) %	$ (1,032)	(5)%	$ (189)	(18)%

* Greater than 100%

Net Sales

Net sales from continuing operations for fiscal 2016 were $20.2 million, a decrease of $1.4 million or 6.5%, compared to net sales of $21.7 million for fiscal 2015.

The decrease in net sales for fiscal 2016 resulted primarily from the non-recurrence of sales to a large national retailer. Decreased sales were also experienced in the catalog, independent and licensed footwear channels, while sales in internet based channel were flat.

Gross Profit

Gross profit from operations for fiscal 2016 increased $146,000 or 2.0% to $7.4 million from $7.3 million when compared to fiscal 2015. Gross profit as a percentage of net sales was 36.7% during fiscal 2016 compared to 33.6% for fiscal 2015.

The 310 basis point improvement in gross profit as a percentage of net sales for fiscal 2016 was produced by an improved channel mix and reduced level of product aired from China to meet anticipated customer demand of licensed footwear.

Cost of goods sold includes all direct costs of products (net of purchase discounts and vendor allowances), allocated overhead (primarily sourcing and indirect production costs), inbound freight and merchandise acquisition costs such as import fees, as well as outbound shipping and handling. The Company's cost of goods sold may not be comparable to those of other entities, since some entities include all of the costs associated with their distribution functions in cost of goods sold while the Company includes these costs in SG&A expenses.

Operating Expenses

Selling, general and administrative expenses, or SG&A, increased $521,000, to $8.1 million during fiscal 2016 compared to $7.5 million for fiscal 2015. SG&A as a percentage of net sales increased to 39.8% for fiscal 2016, compared to 34.8% for fiscal 2015.

The increase in SG&A during 2016 included the $454,000 write off of accounts receivable resulting from the closure of two internet based accounts, as well as a $359,000 increase in salaries in sales and marketing offset in part by a $207,000 decrease in tradeshow and related travel expense.

SG&A consists primarily of the following: compensation, sales and marketing, design and development, professional fees, insurance, depreciation and other operating expenses.

Interest Expense

Interest expense from continuing operations during fiscal 2016 and fiscal 2015 was $590,000, and $776,000, respectively. The decrease in interest expense is related to lower borrowings on the company's revolver with Sterling National Bank and nonrecurring prepaid debt expense with the extinguishment of AloStar Business Credit, LLC credit facility in fiscal 2015.

Liquidity and Capital Resources

Historically, the Company's primary sources of liquidity have been generated from cash flows from operations, the working capital line of credit with its banks, the issuance of debt and other financing alternatives such as leasing. On August 18, 2015, the Company completed the sale of 4,000,000 shares of its common stock at a price of $0.50 per share in a private placement to its shareholders who are "accredited inventors," as defined in Regulation D of the Securities Act of 1933, to fund inventory purchasing in anticipation of increased demand for the Company's occupational and licensed footwear offering. The Company requires cash for inventory purchasing, distribution and selling activities, as well as for general working capital purposes. The Company's need for working capital is seasonal with the greatest requirements existing from December to February, and again between June and August of each year. The Company typically builds up its inventory early during each of these periods to meet customer demand for the Spring/Summer and Fall/Winter selling seasons.

Working Capital

During fiscal 2016 and fiscal 2015, the Company funded its operations with cash generated by operating activities, borrowings from its revolving credit facility, and the sale of 4,000,000 common shares to its shareholders, who are accredited investors. Cash was used to purchase inventory and fund ongoing operating activities. Historically, the Company has also funded its operations through vendor provided credit.

The Company's working capital varies from time to time due to the seasonal requirements of its brands (which have historically been heightened during the first and third quarters), the timing of factory shipments, the need to increase inventories and support an in-stock position in anticipation of customers' orders, and the timing of accounts receivable collections.

As of December 31, 2016 and January 2, 2016, working capital consisted of the following:

	December 31, 2016	January 2, 2016	Increase (Decrease)
		(In thousands)	
Current assets	$ 12,155	$ 13,865	$ (1,710)
Current liabilities	9,117	9,381	(264)
Working capital	$ 3,038	$ 4,484	$ (1,446)

As described below, the primary changes in the components of working capital were to accounts receivable, inventory, revolving line of credit and accounts payable and accrued expenses.

Accounts Receivable

As of December 31, 2016, gross accounts receivable were $3.6 million, a decrease of $504,000 or 12.3% from $4.1 million as of January 2, 2016. The decrease in gross accounts receivable as of December 31, 2016 as compared to January 2, 2016 is consistent with the decrease of $1.4 million in sales and the write off of $454,000 in accounts receivable to bad debt with the closure of two internet based customers.

Inventory

As of December 31, 2016, gross inventory was $9.6 million compared to $10.9 million as of January 2, 2016, a decrease of $1.3 million or 11.8%. The decrease in inventory is primarily associated with reduced buying of core and carry-over styles in the fall and spring 2017 in an effort to improve the inventory turn and increase the number of buys throughout the year.

Revolving Credit Facility

The outstanding balance on the revolving credit facility as of December 31, 2016 was $4.4 million, a decrease of $732,000 or 14.2% when compared to $5.2 million as of January 2, 2016. The decrease in the outstanding balance of the revolving credit facility is primarily associated with reduced inventory fall 2016 and spring 2017 inventory purchasing.

Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses as of December 31, 2016 increased $488,000 to $4.3 million from $3.8 million as of January 2, 2016. The increase in accounts payable and accrued expenses was primarily associated with increased sample costs, amounts due to third party footwear suppliers in China, and other operating expenses that were partly offset by a reduction in accrued in-transit goods liability.

Economic Outlook

While the U.S. economy has steadily improved since the end of the 2009 recession, it has been hampered by a historically lower than normal labor participation rate, stagnate wage growth, and persistent uncertainty in the global economy which has contributed to the cautious outlook in the consumer's confidence. While the U.S. economy has steadily improved over the last several years, and more recently there has been a sharp improvement in consumer confidence, any uncertainty about the current or future economic conditions may cause consumers and retailers to defer purchases or cancel purchase orders for the Company's products in response to tighter credit, decreased cash availability and weakened consumer confidence.

Sale of Equity Securities

On August 18, 2015, the Company completed the sale of 4,000,000 shares of its common stock at a price of $0.50 per share. The sale was made in a private placement offer to its shareholders who are "accredited investors."

The offering was made directly on a best efforts basis without an underwriter or any minimum number of shares that must be sold. The offering commenced on July 28, 2015, and terminated at 5:00 p.m. Eastern Time on August 17, 2015. The shares were issued to accredited investors in private transactions not involving any public offering and exempt from the registration requirements of the Securities Act pursuant to Section 4(a)(2) thereof, and Rule 506(c) of Regulation D thereunder. The offering was open to all shareholders of record as of June 11, 2015, who are accredited investors and currently reside in the United States.

Greenwood Capital, LP, a Massachusetts limited partnership, and MGPLA, LP, a Delaware limited partnership, both managed by Greenwood Investments, Inc. (the “Greenwood Investors”) purchased 3.2 million.

800,000 shares were also purchased by other eligible stockholders, including the Company’s Chairman and CEO, James R. Riedman, who purchased 300,000 shares.

Sterling Loan and Security Agreement

As described in Note 5, “Debt”, on February 2, 2015, the Company and Penobscot entered into a Loan and Security Agreement with STerling Business Credit, LLC, a Delaware limited liability company as administrative agent (“Sterling”), and the lenders party thereto from time to time (the “Sterling” Loan Agreement”). The Sterling Loan Agreement provides for up to $9.0 million in borrowing capacity consisting of a revolving line of credit facility of up to $8.0 million (subject to a borrowing base as defined in the Sterling Loan Agreement) with a five-year maturity (the “RLOC”) and a term loan of $1.0 million (the “Term Loan”). Interest on the principal amount outstanding under the RLOC accrues at a rate equal to the greater of (i) the rate per annum published on each Business Day in the “Money Rates” table of *The Wall Street Journal* as the one-month LIBOR rate, adjusted daily, and (ii) 1.0% (such greater amount, the “LIBOR Rate”) plus 3.75%. Interest on the amount outstanding under the Term Loan accrues at the rate equal to the LIBOR Rate plus 5%. The principal amount of the Term Loan is payable in 36 equal monthly installments of $27,778, together with accrued interest, on the first day of each calendar month beginning March 1, 2015. The obligations of the Company as the borrower under the Sterling Loan Agreement have been guaranteed by Penobscot. As security for the obligations of the Company and Penobscot under the Sterling Loan Agreement, the Company and Penobscot have each granted Sterling (for the benefit of the lenders party to the Sterling Loan Agreement) a security interest in all of their personal property.

Proceeds from the Sterling Loan Agreement were used to pay in full the obligations outstanding under that Loan and Security Agreement dated July 30, 2012 between the Company and AloStar Bank of Commerce, which carried an annual interest rate equal to the LIBOR Rate plus 5.5% and that Loan and Security Agreement dated July 30, 2012 between the Company and Gibraltar Business Capital which carried an annual interest rate of 18.0%.

As a condition to the closing under the Sterling Loan Agreement, the Company also extended from October 30, 2015, until July 31, 2020, the maturity date of the $1,350,000 in aggregate principal amount of its subordinated secured 1% convertible notes held by Greenwood Capital LP.

Finance Authority of Maine Term Loan

As describe in Note 8, “Subsequent Events,” on April 4, 2017, the Company entered into an Equipment Loan with the Finance Authority of Maine (“FAME”) for a five year term loan, collateralized by all machinery, equipment, furniture, furnishings, fixtures, tools and leasehold improvements located at the Company’s Old Town, Maine warehouse and distribution center. The Equipment Loan, consisting of a secured five year term loan in the principal amount of $300,000, bears interest at a fixed per annum rate of 6.0%. Payments of principal and interest in the amount of $5,800 commencing one month from the date entered into and continuing on the same day of each month thereafter until April 4, 2022 (the “Maturity Date”), when, unless sooner paid, the remaining principal and accrued and unpaid interest shall be due and payable in full. The Sterling National Bank Loan Agreement and the Subordinated Loan Agreement were amended in connection with the Equipment Loan to permit the transactions contemplated thereunder. In addition, Sterling National Bank and the Greenwood Parties entered into a separate subordination letter agreement with FAME to permit the repayment of the Equipment Loan and the use of certain equipment as collateral. The proceeds of the FAME loan agreement were used to extinguish the remaining outstanding amount of $73,635 of the FAME loan agreement entered into on November 11, 2013, and other ongoing working capital requirements.

In the absence of a significant decline in sales levels, the Company believes that cash flows from operations, the borrowing capacity of its revolving credit facility, and its access to capital will be sufficient to meet the ongoing needs of its business, anticipated growth, flow of inventory, investment requirements and working capital needs for the next twelve months. In the event we are not able to maintain our anticipated sales levels, we may need additional financing to maintain our operations. If additional future financing is necessary can be no assurance that, if needed, the Company will be able to secure additional debt or equity financing with terms acceptable to it or even at all.

Cash Flows Provided by (Used in) Operations

Continuing Operations

Net cash provided by operating activities from continuing operations during fiscal 2016 was $1.2 million compared to $3.1 million of net cash used in operating activities from continuing operations during fiscal 2015.

Cash provided by operating activities during fiscal 2016 were comprised of a $1.2 million decrease in inventory purchases, a $503,000 decrease in accounts receivable as well as $388,000 increase in accounts payable combined with a $1.2 million net loss during fiscal 2016.

Cash used in operating activities during fiscal 2015 were comprised of a $2.2 million increase in inventory purchases of licensed occupational footwear together with a $1.0 million net loss during the period.

Cash Flows Used In Investing Activities

Net Cash used in investing activities during fiscal 2016 was zero, compared to net cash used in investing activities of $7,000 during fiscal 2015. Net cash of $7,000 used in investing activities resulted from the purchase of equipment for our warehouse facilities in Old Town, Maine.

Cash Flows Used In (Provided by) Financing Activities

Net cash used in financing activities during fiscal 2016 of $1.2 million is primarily the result of borrowings on the Company's revolving credit facility.

Net cash provided by financing activities during fiscal 2015 of $3.1 million consisted of a $1.0 million term note issued with the closing of the new Loan and Security Agreement with Sterling Business Credit, LLC in February 2015 and the Company's completion of the sale of $24,000,000 shares of its common stock

Inflation

The Company believes that the relatively moderate rates of inflation in recent years have not had a significant impact on its net sales or profitability.

Critical Accounting Policies

The Company's accounting policies are more fully described in Note 1 of the Consolidated Financial Statements included in this Annual Report for the fiscal period ended December 31, 2016. As disclosed in Note 1, the Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United

States ("GAAP"). The preparation of the Company's consolidated financial statements requires the Company to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities in the consolidated financial statements and accompanying notes. Although these estimates are based on the Company's knowledge of current events and actions it may undertake in the future, actual results may ultimately differ from these estimates and assumptions. Furthermore, when testing assets for impairment in future periods, if the Company's management uses different assumptions or if different conditions occur, impairment charges may result.

The Company believes that the following discussion addresses its most critical accounting policies, which are those that are most important to the portrayal of its financial condition and results of operations and require the Company's most difficult, subjective and complex judgments.

Revenue Recognition

The Company recognizes revenue from product sales when persuasive evidence of an arrangement exists, products are shipped and the customer takes title and assumes risk of loss, the sales price charged is fixed or determinable and collectability is reasonably assured. Product sales and shipping revenues, net of sales allowances, discounts and return allowances, are recorded when the products are shipped or, in certain situations, upon acceptance by the customer. Allowances for estimated returns are accounted for as reductions to sales, cost of goods sold, accounts receivable and an increase in inventory to the extent such product is resalable. The Company bases its estimates on historical rates of customer returns and allowances, as well as the specific identification of outstanding returns and allowances, which are known to the Company but which have not yet been received or paid. Sales taxes collected from e-commerce customers are excluded from reported sales.

Allowance for Doubtful Accounts

The Company provides a reserve against its accounts receivable for estimated losses that may result from non-collection due to the financial position of its customers. To minimize the likelihood of uncollectibility, customers' credit-worthiness is reviewed periodically based on external credit reporting services and the Company's experience with the account, and it is adjusted accordingly. When a customer's account becomes significantly past due, the Company generally places a hold on the account and discontinues further shipments to that customer, minimizing further risk of loss. The Company determines the amount of the reserve by analyzing known uncollectible accounts, aged receivables, economic conditions in the customers' industries, historical losses and its customers' credit-worthiness. Amounts later determined and specifically identified to be uncollectible are charged or written off against this reserve. In addition to these individual assessments, in general, outstanding trade accounts receivable amounts that are greater than 365 days are fully reserved for and amounts greater than 120 days are 75% reserved for. The Company's level of reserves may fluctuate depending upon all of the factors mentioned above. The Company also reserves for potential trade discounts and deductions for co-op advertising normally taken by its customers, allowances the Company provides to its retail customers to effectively flow goods through the retail channels and an allowance for estimated sales returns.

Historically, actual results in these areas have not been materially different than management's estimates, and the Company does not anticipate that its estimates and assumptions are likely to materially change in the future. However, if the Company incorrectly anticipates trends or unexpected events occur, the Company's results of operations could be materially affected.

Reserve for Obsolete or Slow Moving Inventory

The Company reduces the carrying cost of inventories for obsolete or slow moving items as necessary to properly reflect inventory value. Reserves are estimated based upon inventory on hand, historical sales activity and the expected net realizable value. The Company's analysis includes a review of inventory quantities on hand at period end in relation to year-to-date sales, existing orders from customers and projections for sales in the near future. The net realizable value, or market value, is determined using the Company's estimate of sales prices of such inventory based upon historical sales experience on a style by style basis or, if necessary, through off-price or discount store channels.

Historically, actual results in these areas have not been materially different than the estimates of management and the Company does not anticipate that its estimates and assumptions are likely to materially change in the future. However, the likelihood of any material change is dependent primarily on the Company's expectations of future consumer demand for its footwear. A misinterpretation or misunderstanding of future consumer demand for the Company's footwear or of the economy, or other failure to estimate correctly, could result in inventory valuation changes, either favorably or unfavorably, compared to the requirement determined to be appropriate as of the balance sheet date.

Valuation of Deferred Income Taxes

The Company records a valuation allowance when necessary to reduce its deferred tax assets to the amount that is more likely than not to be realized. The Company evaluates its projections of taxable income to determine the recoverability of its deferred tax assets and the need for a valuation allowance. The Company considers all evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations. As of December 31, 2016 and January 2, 2016, the Company had a full valuation allowance on its deferred tax assets. The likelihood of a material change in the Company's expected realization of its deferred tax assets depends on future taxable income and the effectiveness of the Company's tax planning strategies amongst the various domestic and international tax jurisdictions in which the Company operates.

Recently Adopted Accounting Standards

Debt Issuance Costs

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-03: *Simplifying the Presentation of Debt Issuance Costs,* which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 requires retrospective adoption and is effective for fiscal years beginning after December 15, 2015. In August 2015, the FASB issued ASU 2015-15: *Interest — Imputation of Interest (Subtopic 835-30),* which relates to the presentation of debt issuance costs associated with line-of-credit arrangements. This standard clarifies the guidance set forth in ASU 2015-03, which requires that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from the debt liability rather than as an asset. The new pronouncement clarifies that debt issuance costs related to line-of-credit arrangements could continue to be presented as an asset and be subsequently amortized over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the arrangement. The Company considered this clarification in conjunction with the adoption of ASU 2015-03, which occurred on January 1, 2016. These pronouncements did not have a material impact on the Company's condensed consolidated financial statements. In adopting ASU 2015-15, the Company elected to present debt issuance costs related to line-of-credit arrangements as an asset.

Share-Based Payments

In June 2014, the FASB issued ASU 2014-12 in response to the Emerging Issues Task Force consensus on Issue 13-D. The ASU clarifies that entities should treat performance targets that can be met after the requisite service period of a share-based payment award as performance conditions that affect vesting. Therefore, an entity would not record compensation expense related to an award for which transfer to the employee is contingent on the entity's satisfaction of a performance target until it becomes probable that the performance target will be met. The ASU does not contain any new disclosure requirements. This ASU is effective for all entities for reporting periods (including interim periods) beginning after December 15, 2015. On January 1, 2016, the Company adopted this pronouncement, which did not have a material impact on its condensed consolidated financial statements.

Recently Issued Accounting Standards - Not Yet Adopted

Statement of Cash Flows - Classification

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, which provides guidance for how certain transactions are classified in the statement of cash flows. This standard requires a retrospective transition method to each period presented and is effective for reporting periods beginning after December 15, 2017, with early adoption permitted. The Company is currently assessing the impact of the adoption of this standard on its condensed consolidated financial statements.

Stock Compensation

In March 2016, the FASB issued ASU No. 2016-09, *Compensation — Stock Compensation (Topic 718),* which is intended to increase simplification of accounting for equity share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This standard is effective for annual periods (including interim periods) beginning after December 15, 2016, with early adoption permitted.

Amendments related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements, forfeitures, and intrinsic value should be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. Amendments related to the presentation of employee taxes paid on the statement of cash flows when an employer withholds shares to meet the minimum statutory withholding requirement should be applied retrospectively. Amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement and the practical expedient for estimating the expected term should be applied prospectively. An entity may elect to apply the amendments related to the presentation of excess tax benefits on the statement of cash flows using either a prospective transition method or a retrospective transition method. The Company is currently assessing the impact of adoption of this standard on its condensed consolidated financial statements.

Prepaid Stored-Value Products

In March 2016, the FASB issued ASU No. 2016-04, *Liabilities — Extinguishment of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products.* This update aligns recognition of the financial liabilities related to prepaid stored-value products (for example, prepaid gift cards), with Topic 606, *Revenue from Contracts with Customers,* for non-financial liabilities. In general, certain of these liabilities may be extinguished proportionally in earnings as redemptions occur, or when redemption is remote if issuers are not entitled to the unredeemed stored value. This standard is effective for annual periods (including interim periods) beginning after December 15, 2017, with early adoption permitted. At adoption, this update will be applied either using a modified retrospective transition method by means of a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year in which the guidance is effective or retrospectively to each period presented. The Company is currently assessing the adoption method and the impact that adopting this new accounting standard will have on its condensed consolidated financial statements.

Leases

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842),* which is intended to increase transparency and comparability of accounting for lease transactions. This update revises accounting for operating leases by a lessee, among other changes, and requires a lessee to recognize a liability to make lease payments and an asset representing a company’s right to use the underlying asset for the lease term in the balance sheet. The distinction between finance and operating leases has not changed and the update does not significantly change the effect of finance and operating leases on the statement of operations. This standard is effective for annual periods (including interim periods) beginning after December 15, 2019, with early adoption permitted. At adoption, this update will be applied using a modified retrospective approach. The Company is currently assessing the impact of adoption of this standard on its condensed consolidated financial statements.

Financial Instruments

In January 2016, the FASB issued ASU 2016-01: *Financial Instruments — Overall: Recognition and Measurement of Financial Assets and Financial Liabilities.* The pronouncement requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset, and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The ASU requires the adoption method by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The amendments relating to equity securities without readily determinable fair values (including disclosure requirements) will be applied prospectively to equity investments that exist as of the date of adoption. These changes become effective for fiscal years beginning after December 15, 2017. The expected adoption method is being evaluated by the Company and is not expected to have a significant impact on its condensed consolidated financial statements.

Inventory

In July 2015, the FASB issued ASU 2015-11: *Simplifying the Measurement of Inventory*, which modifies existing requirements regarding measuring inventory at the lower of cost or market. Specifically, this standard eliminates the need to determine and consider replacement cost or net realizable value less an approximately normal profit margin when measuring inventory. This ASU requires a prospective adoption method and is effective prospectively after December 15, 2016, with early adoption permitted. The Company is currently evaluating the impact that this pronouncement will have on its condensed consolidated financial statements.

Revenue Recognition

In May 2014, the FASB issued ASU 2014-09: *Revenue from Contracts with Customers (Topic 606)*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that "an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services." ASU 2014-09 becomes effective for reporting periods (including interim periods) beginning after December 15, 2018. Early application is permitted for reporting periods (including interim periods) beginning after December 15, 2016. This new standard permits the use of either the retrospective or cumulative effect transition method. The Company is currently evaluating the impact that this pronouncement will have on its condensed consolidated financial statements. The Company has not yet selected a transition method or determined the effect of the standard on financial reporting once the standard is effective.

In May 2016, the FASB issued ASU 2016-12: *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*, which provides narrow scope improvements and practical expedients related to ASU 2014-09: *Revenue from Contracts with Customers (Topic 606)*. The purpose of ASU 2016-12 is to clarify certain narrow aspects of Topic 606 such as assessing the collectability criterion, presentation of sales taxes and other similar taxes collected from customers, noncash consideration, contract modifications at transition, completed contracts at transition, and technical correction. The standard has the same effective date as ASU 2014-09 described above. The Company is currently evaluating the impact that this pronouncement will have on its condensed consolidated financial statements. The Company has not yet selected a transition method or determined the effect of the standard on financial reporting once the standard is effective.

Off-Balance Sheet Arrangements

Other than operating leases, entered into from time to time in the normal course of business, and as discussed here and described in Note 3 of the notes to the consolidated financial statements, the Company does not have any other off-balance sheet arrangements. The Company does not believe that these operating leases or the licensing agreement are material to its current or future financial condition, results of operations, liquidity, capital resources or capital expenditures.