

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

FORM 10-K

(Mark One)

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

For the fiscal year ended January 29, 2005

Or

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

Commission File Number	Registrant, State of Incorporation Address and Telephone Number	I.R.S. Employer Identification No.
333-42427	J. CREW GROUP, INC. (Incorporated in New York) 770 Broadway New York, New York 10003 Telephone: (212) 209-2500	22-2894486
333-42423	J. CREW OPERATING CORP. (Incorporated in Delaware) 770 Broadway New York, New York 10003 Telephone: (212) 209-2500	22-3540930

Securities Registered Pursuant to Section 12(b) of the Act: None

Securities Registered Pursuant to Section 12(g) of the Act: None

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of each registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by a check mark whether either of the registrants is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The common stock of each registrant is not publicly traded. Therefore, the aggregate market value is not readily determinable.

Outstanding at April 1, 2005:

J. Crew Group, Inc.	12,473,306 shares of common stock, par value \$.01 per share
J. Crew Operating Corp.	100 shares of common stock, par value \$.01 per share (all of which are owned indirectly by J.Crew Group, Inc.)

This Annual Report on Form 10-K is a combined report being filed by two different registrants: J.Crew Group, Inc. and J.Crew Operating Corp. (a wholly-owned indirect subsidiary of J.Crew Group, Inc.). The information contained herein relating to each individual registrant is filed by such registrant on its own behalf. No registrant makes any representation as to information relating to any other registrant.

Documents incorporated by reference: None

J.Crew Operating Corp. meets the conditions set forth in General Instruction (I)(1)(a) and (b) of the Form 10-K and is therefore filing this Form 10-K with the reduced disclosure format.

FILING FORMAT

This Annual Report on Form 10-K is a combined report being filed by two different registrants: J.Crew Group, Inc. ("Group") and J.Crew Operating Corp., a wholly-owned indirect subsidiary of Group ("Operating"). Except where the content clearly indicates otherwise, any references in this report to the "Company", "J.Crew" or "Group" include all subsidiaries of Group, including Operating. Operating does not make any representations as to the information contained in this report in relation to Group and its subsidiaries other than Operating.

References herein to fiscal years are to the fiscal years of Group and Operating, which end on the Saturday closest to January 31 in the following calendar year for fiscal years 2000, 2001, 2002, 2003 and 2004. Accordingly, fiscal years 2000, 2001, 2002, 2003 and 2004 ended on February 3, 2001, February 2, 2002, February 1, 2003, January 31, 2004 and January 29, 2005. All fiscal years for which financial information is included are 52 weeks, except fiscal year 2000 which had 53 weeks.

PART I

BUSINESS

In this section, "we," "us" and "our" refer to Group and our wholly owned subsidiaries, including Operating.

General

We are a nationally recognized retailer of women's and men's apparel, shoes, and accessories sold under the "J.Crew" brand name. Started in 1983, we have built and reinforced our brand name and image through both the circulation of catalogs that use magazine-quality photography to portray a classic American perspective and aspirational lifestyle and the operation of our stores and internet website. We believe that the "J. Crew" brand name is widely recognized as an iconic American brand known for its classic styles. We offer a full line of men's and women's clothing, including basic durables, wear to work, wedding attire, swimwear, loungewear, accessories and shoes to meet our customers' lifestyle needs.

J. Crew products are distributed through our retail and factory outlet stores, our catalog and our internet website located at www.jcrew.com. As of January 29, 2005, we operated 156 retail stores and 41 factory outlet stores in the United States. We believe that our customer base consists primarily of college-educated, professional and upscale men and women who in our experience have demonstrated strong brand loyalty and a tendency to make repeated purchases. In addition, J.Crew products are distributed through 43 freestanding and shop-in-shop stores in Japan under a licensing agreement with Itochu Corporation.

We have two major operating divisions: J.Crew Retail (consisting of our retail and factory outlet stores) and J.Crew Direct (consisting of our catalog and Internet website), each of which operate under the J.Crew brand name. In fiscal 2004, products sold under the J.Crew brand contributed \$778.3 million in revenues, comprised of:

- \$579.8 million from J.Crew Retail; and
- \$198.5 million from J.Crew Direct.

In addition, in fiscal 2004, we generated other revenues of \$25.9 million, consisting principally of shipping and handling fees derived from J.Crew Direct.

Group was incorporated in the State of New York in 1988 and Operating was incorporated in the State of Delaware in 1997. Group is the sole member of J.Crew Intermediate LLC, a Delaware limited liability company ("Intermediate"), and Intermediate owns 100% of the outstanding shares of Operating. Our principal executive offices are located at 770 Broadway, New York, NY 10003, and our telephone number is (212) 209-2500.

See "Forward Looking Statements and Risk Factors".

Merchandising and Design

Over time, our merchandising strategy has evolved from providing unisex products to creating full lines of men's and women's clothing, shoes and accessories. This strategy had the effect of increasing overall J.Crew brand sales volume and significantly increasing revenues from sales of women's apparel to 75% of J.Crew brand sales in fiscal 2004.

All of our products are designed by an in-house design staff to reflect a classic, clean aesthetic that is consistent with our American lifestyle brand image. Design teams are formed around J.Crew product lines and categories to develop concepts, themes and products for each of our J.Crew businesses. Our technical design teams develop construction and fit specifications for every product to ensure quality

workmanship and consistency across product lines. These teams work in close collaboration with the merchandising, production and quality assurance staffs in order to gain market and other input and ensure quality of the J.Crew products.

Sourcing and Production

Our merchandise is produced for us by a variety of manufacturers in 35 countries. We do not own or operate any manufacturing facilities and instead contract with third-party vendors for production of our merchandise. In fiscal 2004, approximately 77% of our merchandise was sourced in Asia, 8% was sourced in the United States and 15% was sourced in Europe and other regions. Any event causing a sudden disruption of manufacturing or imports from Asia, including the imposition of additional import restrictions, could have a material adverse impact on our operations. In addition, one vendor supplies approximately 15% of our merchandise, but we believe that the loss of this vendor would not have a material adverse impact on our ability to source our products. Substantially all of our foreign purchases are negotiated and paid for in U.S. dollars.

We cannot predict whether any of the countries in which our merchandise is currently produced or may be produced in the future will be subject to additional trade restrictions imposed by the United States and other foreign governments, nor can we predict the likelihood, type or effect of any such restrictions. Trade restrictions, including increased tariffs or quotas, against apparel and other items sold by us could increase the cost or reduce the supply of merchandise available to us and adversely affect our business, financial condition and results of operations. Our sourcing operations may also be adversely affected by political and financial instability in any country in which our goods are produced or by acts of war or terrorism in the United States or worldwide to the extent these acts impact the production, shipment or receipt of merchandise. Sourcing operations may also be adversely affected by significant fluctuation in the value of the U.S. dollar against foreign currencies or restrictions on the transfer of funds. See "Forward-Looking Statements and Risk Factors".

Distribution

We operate one primary customer call center and two distribution facilities for our operations. We own a 406,500 square foot facility in Lynchburg, Virginia that contains our customer call center, order fulfillment operations for J.Crew Direct and distribution operations for our factory outlet stores. This facility employs approximately 500 full and part-time employees during our non-peak season and additional employees during our peak season. We also own a 192,500 square foot facility in Asheville, North Carolina that contains our distribution operations for our retail stores. This facility employs approximately 100 full and part-time employees during our non-peak season and additional employees during our peak season. To enhance efficiency, each facility is fully equipped with an automated warehouse locator system and inventory bar coding system. In addition, our facility in Lynchburg has automated packing and shipping sorters. Merchandise is shipped to our customers via the United States Postal Service and Federal Express. We believe that our customer call center, order fulfillment operations and distribution operations are designed to handle customer orders and distribute merchandise to stores in a customer-friendly, efficient and cost-effective manner.

Information Systems

Our management information systems are designed to provide, among other things, comprehensive order processing, production, accounting and management information for the marketing, manufacturing, importing and distribution functions of our business. We have installed an SAP enterprise resource planning system for our information technology requirements. We have point-of-sale registers in our retail and factory outlet stores that enable us to track inventory from store receipt to final sale on a real-time basis. We believe our merchandising and financial systems, coupled with our point-of-sale registers and software programs, allow for rapid stock replenishment, concise

merchandise planning and real-time inventory accounting practices. Our telephone and telemarketing systems, warehouse package sorting systems, automated warehouse locator and inventory bar coding systems utilize advanced technology. These systems have provided us with a number of benefits in the form of enhanced customer service, improved operational efficiency and increased management control and reporting. In addition, our real-time inventory systems provide inventory management on a stock keeping unit basis and allow for an efficient fulfillment process.

Trademarks and Licensing

The "J.Crew" trademark and variations thereon, and certain other trademarks, are registered or are subject to pending trademark applications with the United States Patent and Trademark Office and with the registries of many foreign countries. We believe that our trademarks have significant value and we intend to continue to vigorously protect them against infringement.

In addition, we license our "J.Crew" trademark to Itochu Corporation in Japan for which we receive percentage royalty fees. Under the license agreement, we retain a high degree of control over the manufacture, design, marketing and sale of merchandise by Itochu Corporation under the J.Crew trademark. This agreement expires in January 2007. In fiscal 2004, licensing revenues totaled \$2.8 million.

Employees

As of January 29, 2005, we had approximately 6,100 employees, of whom approximately 2,200 were full-time employees and 3,900 were part-time employees. In addition, approximately 1,900 employees are hired on a seasonal basis to meet demand during the peak season. None of our employees are represented by a union. We believe that our relationship with our employees is good.

Competition

All aspects of our business are highly competitive. We compete primarily with specialty brand retailers, other catalog and internet operations, department stores and mass merchandisers that offer similar merchandise. We believe that the principal bases upon which we compete are quality, design, efficient service, selection and price. Many of our competitors are substantially larger, have a more established retail store presence and experience and have greater financial, marketing and other resources than us. There is no assurance that we will be able to successfully compete with our competitors in the future. In addition, our business is sensitive to a number of factors that could affect the level of consumer spending, including adverse economic conditions, the levels of disposable consumer income, consumer confidence and interest rates. See "Forward-Looking Statements and Risk Factors".

Our Business

J. Crew Retail

J.Crew Retail consists of our retail and factory outlet store operations. During fiscal 2004, J.Crew Retail generated revenues of \$579.8 million, representing 72.1% of our total revenues.

As of January 29, 2005, we operated 156 retail stores and 41 factory outlet stores throughout the United States. Our retail stores are located in upscale regional malls, lifestyle centers, shopping centers and street locations. Our factory outlet stores are generally located in major regional outlet centers. Store locations are determined based on several factors, including geographic location, demographic information, presence of anchor tenants in mall locations and proximity to other specialty retail stores. All of our stores are designed in-house and fixtured to create a distinctive J.Crew environment and our store associates are trained to maintain high standards of visual presentation and customer service.

All stores that were open during all of fiscal 2004 averaged \$2.9 million per store in sales and produced sales per gross square foot of \$397. Our retail and factory outlet stores have an average size of 7,400 total square feet. The table below highlights certain information regarding our retail and factory outlet stores open during the five years ended January 29, 2005:

Fiscal Year	Stores Open At Beginning of Fiscal Year	Stores Opened During Fiscal Year	Stores Closed During Fiscal Year	Stores Open at End of Fiscal Year	Total Square Footage (in thousands)	Average Store Square Footage
2000	123	24	1	146	1,094	7,496
2001	146	34	3	177	1,314	7,425
2002	177	18	1	194	1,436	7,402
2003	194	4	2	196	1,447	7,381
2004	196	5	4	197	1,457	7,394

J.Crew Direct

J.Crew Direct consists of our catalog and internet website operations. During fiscal 2004, J.Crew Direct generated \$198.5 million in revenues, including \$76.5 million from the catalog and \$122.0 million from the internet website, representing 24.7% of our total revenues.

We believe we have distinguished ourselves from other catalog retailers by our catalog which utilizes magazine-quality photography to depict an aspirational lifestyle image. In fiscal 2004, we distributed 32 catalog editions with a circulation of approximately 50 million and pages circulated of approximately 5.4 billion. This represented an increase from fiscal 2003 in which we distributed 28 catalog editions, but reflects a decrease in circulation as our fiscal 2003 circulation was approximately 53 million and pages circulated were approximately 5.8 billion.

We focus on continually improving the segmentation of customer files and the acquisition of additional customer names. In fiscal 2004, approximately 58% of J.Crew Direct revenues were generated by customers who had made a purchase from any J.Crew catalog or on our internet website in the prior 12 months. We segment our customer files and tailor our catalog offerings to address the different product needs of our customer segments. To increase core catalog productivity and improve the effectiveness of marginal and prospecting circulation, each customer segment is offered appropriate catalog editions. We also acquire new names from various sources, including our retail stores, our internet website, list rentals and exchanges with other catalog companies. Telephones are also installed in most of our stores with direct access to our customer call center to allow customers in our stores to order catalog-specific or out-of-stock items.

All creative work on the catalogs is coordinated by J.Crew personnel to maintain and reinforce our brand image. Photography is executed both on location and in studios, and creative design and copy writing are executed on a desktop publishing system. Digital images are transmitted directly to outside printers, thereby reducing lead times and improving reproduction quality.

We do not have long-term contracts with paper mills. Projected paper requirements are communicated on an annual basis to paper mills to ensure the availability of an adequate supply. We believe that our long-standing relationships with a number of the largest coated paper mills in the United States allow us to purchase paper at favorable prices commensurate with the volume of our purchases.

In 1996, we launched our internet website located at www.jcrew.com, making J.Crew merchandise available to our customers over the internet. In fiscal 2004, our website logged over 48 million unique visitors, an increase of 26% over our fiscal 2003 visitors of 38 million, and represented 62% of the J.Crew Direct business. We design and operate our website using an in-house technical staff and our

website emphasizes simplicity and ease of customer use while integrating the J.Crew brand's aspirational lifestyle imagery used in the catalog.

Available Information

We are subject to the informational requirements of the Securities Exchange Act of 1934 (Exchange Act). We therefore file periodic reports and other information with the Securities and Exchange Commission (SEC). Such reports may be obtained by visiting the Public Reference Room of the SEC at 450 Fifth Street NW, Washington, D.C. 20549, or by calling the SEC at (800) SEC-0330. In addition, the SEC maintains an internet website (www.sec.gov) that contains reports, proxy information statements and other information regarding issuers that file electronically.

Our filings under the Exchange Act (including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to these reports) are also available free of charge on our internet website at www.jcrew.com. These reports are available as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. The reference to the Company's website address does not constitute incorporation by reference of the information contained on the website, and the information contained on the website is not part of this document.

ITEM 2. PROPERTIES

We are headquartered in New York City. Our headquarter offices are leased under a lease agreement expiring in 2012, with an option to renew thereafter. We own two facilities: a 406,500-square-foot customer contact call center, order fulfillment and distribution center in Lynchburg, Virginia and a 192,500-square-foot distribution center in Asheville, North Carolina.

As of January 29, 2005, we operated 156 J.Crew retail stores and 41 factory outlet stores in 39 states and the District of Columbia. All of the retail and factory outlet stores are leased from third parties, and the leases in most cases have terms of 10 to 12 years, with options to renew for periods typically ranging from five to ten years. As a general matter, the leases contain standard provisions concerning the payment of rent, events of default and the rights and obligations of each party. Rent due under the leases is generally comprised of annual base rent plus a contingent rent payment based on the store's sales in excess of a specified threshold. Some of the leases also contain early termination options, which can be exercised by us or in some cases the landlord under certain conditions. The leases also generally require us to pay real estate taxes, insurance and certain common area costs. Substantially all of the leases are guaranteed by us.

The table below sets forth the number of stores by state operated by us in the United States as of January 29, 2005.

	Retail Stores	Factory Stores	Total Number of Stores
Alabama	2	1	3
Arizona	4	—	4
California	20	3	23
Colorado	4	2	6
Connecticut	6	1	7
Delaware	—	1	1
Florida	4	3	7
Georgia	4	2	6
Illinois	9	—	9
Iowa	1	—	1
Indiana	1	1	2
Kansas	1	—	1

Kentucky	2	—	2
Louisiana	1	—	1
Maine	—	2	2
Maryland	3	1	4
Massachusetts	6	2	8
Michigan	6	1	7
Minnesota	4	—	4
Missouri	2	1	3
Nevada	1	—	1
New Hampshire	1	2	3
New Jersey	9	1	10
New Mexico	1	—	1
New York	16	4	20
North Carolina	4	—	4
Ohio	6	—	6
Oklahoma	2	—	2
Oregon	2	—	2
Pennsylvania	8	3	11
Rhode Island	1	—	1
South Carolina	2	2	4
Tennessee	3	1	4
Texas	6	2	8
Utah	2	—	2
Vermont	1	1	2
Virginia	5	2	7
Washington	3	1	4
Wisconsin	1	1	2
District of Columbia	2	—	2
Total	156	41	197

ITEM 3. LEGAL PROCEEDINGS

Charles E. Hill & Associates, Inc., or Hill, filed a lawsuit on August 16, 2002 in the U. S. District Court for the Eastern District of Texas against us and seventeen other defendants, primarily large retailers, alleging infringement of three patents registered to Hill relating to electronic catalog systems and methods for processing data at a remote location and updating and displaying that data. The suit seeks an injunction against continuing infringement, unspecified damages, including treble damages for willful infringement, and interest, costs, expenses and fees. We believe that we have meritorious defenses and intend to defend ourselves vigorously.

In addition, we are subject to various legal proceedings and claims that arise in the ordinary conduct of our business. Although the outcome of these other claims cannot be predicted with certainty, management does not believe that the ultimate resolution of these matters will have a material adverse effect on our financial condition or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the quarter ended January 29, 2005.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

There is no established public trading market for Group or Operating common stock. As of April 1, 2005, there were 54 shareholders of record of the Group common stock. See "Item 12. Security Ownership of Certain Beneficial Owners and Management" for a discussion of the ownership of Group. Operating is a wholly-owned indirect subsidiary of Group.

Group has not paid cash dividends on its common stock and does not anticipate paying any such dividends in the foreseeable future. Operating may from time to time pay cash dividends on its common stock to permit Group to make required payments relating to its outstanding 13¹/₈% Senior Discount Debentures due 2008.

Our amended and restated credit facility with Wachovia Capital Markets LLC, as arranger, Wachovia Bank National Association, as administrative agent, Bank of America N.A., as syndication agent, and Congress Financial Corporation, as collateral agent, and a syndicate of lenders (Amended Wachovia Credit Facility) and the Indenture relating to Group's 13¹/₈% Senior Discount Debentures due 2008 (Group Indenture) prohibit the payment of dividends by Group on shares of common stock (other than dividends payable solely in shares of capital stock of Group). Additionally, because Group is a holding company, its ability to pay dividends is dependent upon the receipt of dividends from its direct and indirect subsidiaries. Each of the Amended Wachovia Credit Facility, the Group Indenture and the Indenture relating to Operating's 9³/₄% Senior Subordinated Notes due 2014 contains covenants that impose substantial restrictions on Operating's ability to pay dividends or make distributions to Group.

Equity Compensation Plan Information

The following table summarizes information about the Amended and Restated J. Crew Group, Inc. 1997 Stock Option Plan and the J.Crew Group, Inc. 2003 Equity Incentive Plan (2003 Plan), as of January 29, 2005. Our shareholders have approved both of these plans.

(c)			
Plan Category	(a) Number of Securities to be Issued Upon Exercise of Outstanding Options Warrants and Rights	(b) Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column(a))
Equity Compensation Plans Approved by Shareholders	4,582,265	\$ 13.15	675,171
Equity Compensation Plans Not Approved by Shareholders	—	N/A	—
TOTAL	4,582,265	13.15	675,171

In addition to options, the 2003 Plan authorizes the issuance of restricted Group common stock. The 2003 Plan contains a sub-limit of 1,450,724 shares on the aggregate number of shares of restricted Group common stock that may be issued, of which 1,340,979 shares are outstanding and 109,745 shares are available for grant as of January 29, 2005.

ITEM 6. SELECTED FINANCIAL DATA

The following table sets forth selected consolidated historical income statement, balance sheet and operating data of the Company. The selected income statement and balance sheet data for each of the five fiscal years ended January 29, 2005 are derived from the Consolidated Financial Statements of the Company, which have been audited by KPMG LLP, independent auditors. The data presented below should be read in conjunction with the Consolidated Financial Statements, including the related Notes thereto, included herein, the other financial information included herein, and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Fiscal Year Ended				
	February 3, 2001(a)	February 2, 2002	February 1, 2003	January 31, 2004	January 29, 2005
(\$ in thousands, except per square foot data)					
Income statement data:					
Revenues	\$ 825,975	\$ 777,940	\$ 768,344	\$ 689,965	\$ 804,216
Cost of goods sold(b)	458,205	454,491	472,262	440,276	478,829
Selling, general and administrative expenses	307,569	303,448	301,718	280,464	287,745
Charges incurred in connection with discontinuance of Clifford & Wills	4,130	—	—	—	—
Income/(loss) from operations	56,071	20,001	(5,636)	(30,775)	37,642
Interest expense—net	36,642	36,512	40,954	63,844	87,571
(Gain) loss on debt refinancing	—	—	—	(41,085)	49,780
Insurance proceeds	—	—	(1,800)	(3,850)	—
Provision (benefit) for income taxes	7,500	(5,500)	(4,200)	500	600
Net income (loss)	\$ 11,929	\$ (11,011)	\$ (40,590)	\$ (50,184)	\$ (100,309)
Balance sheet data (at period end):					
Cash and cash equivalents	\$ 32,930	\$ 16,201	\$ 18,895	\$ 49,650	\$ 23,647
Working capital	49,482	39,164	38,015	46,217	12,168
Total assets	389,861	401,320	348,878	297,611	278,194
Total long-term debt and preferred stock	464,310	510,147	556,038	609,440	669,733
Stockholders' deficit	\$ (278,347)	\$ (319,043)	\$ (391,663)	\$ (468,066)	\$ (581,712)
Operating data:					
Revenues:					
J.Crew Retail	\$ 502,898	\$ 483,083	\$ 484,292	\$ 487,092	\$ 579,793
J.Crew Direct					
Catalog	177,535	135,353	108,531	61,883	76,548
Internet	107,225	122,844	139,456	111,653	121,954
	284,760	258,197	247,987	173,536	198,502
Other	38,317	36,660	36,065	29,337	25,921
Total revenues	\$ 825,975	\$ 777,940	\$ 768,344	\$ 689,965	\$ 804,216
J.Crew Retail:					
Sales per gross square foot(c)	\$ 494	\$ 406	\$ 351	\$ 337	\$ 397
Number of stores open at end of period	146	177	194	196	197
Comparable store sales change(d)	0.7%	(14.5)%	(11.2)%	(2.5)%	16.4%
J.Crew Direct:					
Number of catalogs circulated (in thousands)	73,000	71,000	66,000	53,000	50,000
Number of pages circulated (in millions)	8,700	8,300	7,800	5,800	5,400
Depreciation and amortization	\$ 28,670	\$ 39,963	\$ 43,197	\$ 43,075	\$ 37,061
Capital expenditures:					
New store openings	\$ 30,219	\$ 36,859	\$ 17,202	\$ 5,663	\$ 5,910
Other	25,475	25,003	9,718	4,245	7,521
Total capital expenditures:	\$ 55,694	\$ 61,862	\$ 26,920	\$ 9,908	\$ 13,431

- (a) The fiscal year 2000 consisted of 53 weeks compared to 52 weeks in all other fiscal years. Net sales for the fifty-third week increased fiscal 2000 sales by \$10.8 million.
- (b) Includes buying and occupancy costs.
- (c) Includes stores that have been opened for a full twelve month period.
- (d) Comparable store sales excludes the sales of stores that were not open during the same period in the prior year.

Forward Looking Statements and Risk Factors

Certain statements in this Annual Report on Form 10-K under the captions "Business," "Selected Financial Data," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Financial Statements and Supplementary Data" and elsewhere constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. We may also make written or oral forward-looking statements in our periodic reports to the Securities and Exchange Commission on Forms 10-Q, 8-K, etc., in press releases and other written materials and in oral statements made by our officers, directors or employees to third parties. Statements that are not historical facts, including statements about our beliefs and expectations, are forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of we, or industry results, to differ materially from historical results, any future results, performance or achievements expressed or implied by such forward-looking statements. Such risks and uncertainties include, but are not limited to:

- competitive pressures in the apparel industry;
- changes in levels of consumer spending or preferences in apparel and acceptance by customers of our products;
- overall economic conditions, governmental regulations and trade restrictions, domestic and foreign;
- acts of war or terrorism in the United States or worldwide;
- political or financial instability in the countries where our goods are manufactured;
- postal rate increases, paper and printing costs;
- availability of suitable store locations at appropriate terms;
- the level of our indebtedness and exposure to interest rate fluctuations;

and other risks and uncertainties described in this report and our other reports and documents filed or which may be filed, from time to time, with the Securities and Exchange Commission. These statements are based on current plans, estimates and projections, and therefore you should not place undue reliance on them. Forward looking statements speak only as of the date they are made and we undertake no obligation to update publicly any of them in light of new information or future events.

We caution that there are important factors, in addition to those listed above, that may cause actual results to differ materially from those contained in forward-looking statements. These factors include the following:

We must successfully gauge fashion trends and changing consumer preferences to succeed.

We believe that our success depends in substantial part on our ability to originate and define product and fashion trends as well as to anticipate, gauge and react to changing consumer demands in a timely manner. There can be no assurance that we will be successful in this regard. We attempt to reduce the risks of changing fashion trends and product acceptance by devoting a substantial portion of our product line to basic durables which are not significantly modified from year to year. Nevertheless, if we misjudge the market for our products, we may be faced with significant excess inventories for some products and missed opportunities with others.

The fashion and apparel industry is highly competitive.

The fashion and apparel industry is highly competitive. We compete primarily with other catalog operations, specialty brand retailers, department stores, mass merchandisers and Internet businesses that engage in the retail sale of men's and women's apparel, accessories, footwear and general merchandise. We believe that the principal bases upon which we compete are quality, design, efficient service, selection and price. However, many of our competitors are larger and have greater financial,

marketing and other resources, and there can be no assurance that we will be able to compete successfully with them in the future.

We may be substantially more leveraged than certain of our competitors, which may place us at a competitive disadvantage.

Our substantial degree of leverage may limit our flexibility to adjust to changing market conditions, reduce our ability to withstand competitive pressures and make us more vulnerable to a downturn in general economic conditions or our business. Our ability to make scheduled payments or to refinance our debt obligations will depend upon future financial and operating performance of Operating, which will be affected by prevailing economic conditions and financial, business and other factors, certain of which are beyond our control. There can be no assurance that Operating's operating results, cash flow and capital resources will be sufficient for payment of our indebtedness in the future. In the absence of such operating results, cash flow and capital resources, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt service and other obligations, and there can be no assurance as to the timing of such sales or the proceeds that we could realize from such sale. If we are unable to service our indebtedness, we may take actions such as reducing or delaying planned expansion and capital expenditures, selling assets, restructuring or refinancing our indebtedness or seeking additional equity capital. There can be no assurance that any of these actions could be effected on satisfactory terms, if at all.

Competition for qualified personnel is intense in the fashion and apparel industry.

Our ability to anticipate and effectively respond to changing fashion trends depends in part on our ability to attract and retain key personnel in our design, merchandising and marketing staff. Competition for these personnel is intense, and there can be no assurance that we will be able to attract and retain a sufficient number of qualified personnel in the future. We rely, in particular, on the strategic guidance of Millard Drexler, our Chief Executive Officer, and Jeffrey Pfeifle, our President. The loss, for any reason, of the services of either of these individuals could have a material adverse effect on us.

The fashion and apparel industry is cyclical, and decline in consumer spending on apparel and accessories could have an adverse effect on our results of operations.

The industry in which we operate is cyclical. Purchases of apparel and related merchandise is sensitive to a number of factors that influence the levels of general consumer spending, including economic conditions and the level of disposable consumer income, consumer debt, interest rates and consumer confidence. A decline in consumer spending on apparel and accessories could have an adverse effect on our financial condition and results of operations.

Increase in costs of mailing, paper and printing will have an adverse effect on our results of operations.

Postal rate increases and paper and printing costs affect the cost of our catalog and promotional mailings. We rely on discounts from the basic postal rate structure, such as discounts for bulk mailings and sorting by zip code and carrier routes. We are not a party to any long-term contracts for the supply of paper. Our cost of paper has fluctuated significantly, and our future paper costs are subject to supply and demand forces external to our business. Consequently, there can be no assurance that we will not be subject to an increase in paper costs. Future increases in postal rates or paper or printing costs would have a negative impact on our earnings to the extent that we are unable to pass such increases directly to customers or offset such increases by raising selling prices or by implementing more efficient mailings. See "—Our Business—J. Crew Direct."

We rely on foreign sourcing and are subject to a variety of risks associated with doing business abroad.

In fiscal 2004, approximately 92% of our merchandise was sourced from independent foreign factories located primarily in Asia, and many of our domestic vendors import a substantial portion of

their merchandise from abroad. Any event causing a sudden disruption of manufacturing or imports from China, including the imposition of additional import restrictions, could have a material adverse impact on our operations. We have no long-term merchandise supply contracts, and many of our imports are subject to existing or potential duties, tariffs or quotas that may limit the quantity of certain types of goods that may be imported into the United States from countries in those regions. We compete with other companies for production facilities and import quota capacity. Our business is also subject to a variety of other risks generally associated with doing business abroad, such as political instability, currency and exchange risks and potential local issues. Our sourcing operations may also be adversely affected by political and financial instability or health concerns regarding infectious diseases in countries in which our merchandise is produced or acts of war or terrorism in the United States or worldwide, to the extent these acts impact the production, shipment or receipt of merchandise. Our future performance will be subject to such factors, which are beyond our control, and there can be no assurance that such factors would not have a material adverse effect on our financial condition and results of operations.

Trade restrictions, including increased tariffs or quotas, against apparel and other items sold by us could increase the cost or reduce the supply of merchandise available to us and adversely affect our business, financial condition and results of operations. The United States has agreed, as of January 1, 2005, to a phase out of import quotas for WTO member countries. This should improve flexibility in importing textile and apparel products from WTO member countries. However, any flexibility resulting from this agreement may be eliminated if new restrictions are imposed on the import of apparel from China. In addition, a number of pending applications have been made to U.S. government agencies to delay the elimination of certain quota categories at January 1, 2005. The outcome of these applications, plus other possible efforts to impede the elimination of quotas, could have a significant impact on worldwide sourcing patterns in 2005. The extent of this impact, if any, and the possible effect on our purchasing patterns and costs, cannot be determined at this time. We cannot predict whether any of the countries in which our merchandise currently is manufactured or may be manufactured in the future will be subject to additional trade restrictions imposed by the United States and other foreign governments, including the likelihood, type or effect of any such restrictions. Trade restrictions, including increased tariffs or quotas, embargoes, safeguards and customs restrictions, against apparel items, as well as U.S. or foreign labor strikes, work stoppages or boycotts, could increase the cost or reduce the supply of apparel available to we and adversely affect its business, financial condition and results of operations. See "—Sourcing and Production."

We require our licensing partner and independent manufacturers to operate in compliance with applicable laws and regulations.

While our internal and vendor operating guidelines promote ethical business practices, we do not control such manufacturers or their labor practices. Violation of labor or other laws by our independent manufacturers or our licensing partner, or the divergence of an independent manufacturer's or our licensing partner's labor practices from those generally accepted as ethical in the United States, could have a material adverse effect on our financial condition and results of operations if, as a result of such violation, we were to incur substantial liability or attract negative publicity that damaged our brand.

Success of J. Crew Retail growth strategy remains uncertain.

We intend to expand our base of J. Crew Retail stores as part of our growth strategy. There can be no assurance that this strategy will be successful. Our success depends, in part, on our ability to improve sales and margins at our stores. Actual number and type of such stores to be opened and their success will be dependent upon a number of factors, including, among other things, the ability to manage such expansion and hire and train qualified associates, the availability of suitable store locations and the negotiation of acceptable lease terms for new locations and upon lease renewals for existing locations. There can be no assurance that we will be able to open and operate new stores on a timely or profitable basis. See "Management's Discussion and Analysis of Financial Condition and

Results of Operations of Holdings" and "Our Business—J. Crew Retail." We believe that the opening of J. Crew Retail stores has diverted some revenues from the J. Crew Direct operations. There can be no assurance that future store openings will not continue to have such an effect.

Our quarterly results of operations fluctuate significantly due to seasonality and a variety of other factors.

We experience seasonal fluctuations in revenues and operating income, with a disproportionate amount of our revenues and a majority of our income from operations typically realized during the fourth quarter of each fiscal year. Revenues and income from operations are generally weakest during the first and second quarters of each fiscal year. As a result of this seasonality, sales during the third and fourth fiscal quarters cannot be used as accurate indicators for our annual results. In addition, any factors negatively affecting us during the third and fourth fiscal quarters of any year, including adverse weather or unfavorable economic conditions, could have a material adverse effect on its financial condition and results of operations for the entire year. Also, in order to prepare for our peak shopping seasons, we must order and keep in stock significantly more merchandise than we would carry at other times of the year. Any unanticipated decrease in demand for our products during our peak shopping seasons could require us to sell excess inventory at a substantial markdown, which could reduce our net sales and gross margins and negatively impact our profitability. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Seasonality." Our quarterly results of operations may also fluctuate significantly as a result of a variety of other factors, including the timing of new store openings and of catalog mailings, and the revenues contributed by new stores, merchandise mix and the timing and level of markdowns.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This discussion summarizes the significant factors affecting our consolidated operating results, financial condition and liquidity during the three-year period ended January 29, 2005. You should read the following discussion and analysis in conjunction with our audited consolidated financial statements for the three-year period ended January 29, 2005 and the related notes thereto included herein.

Management's discussion and analysis of the results of operations are provided solely with respect to Operating and its subsidiaries since substantially all of the Company's operations are conducted by Operating. However, Group has additional debt securities that are outstanding. Accordingly, information with respect to interest expense of Group is also provided herein. The discussion of liquidity and capital resources pertains to Group and its consolidated subsidiaries, including Operating.

Management Overview

The fashion and apparel industry is highly competitive. We compete primarily with specialty brand retailers, department stores, other catalog operations, and internet businesses that engage in the retail sale of men's and women's apparel, accessories, footwear and similar merchandise. We believe that the principal bases upon which we compete are quality, design, efficient service, selection and price. We believe that our success depends in substantial part on our ability to originate and define product and fashion trends as well as to anticipate, gauge and react to changing consumer demands in a timely manner.

The industry in which we operate is cyclical. Purchases of apparel and related merchandise are sensitive to a number of factors that influence the levels of consumer spending including economic conditions and the level of disposable consumer income, consumer debt, interest rates and consumer confidence. The economic environment in 2002 had a negative impact on our sales and required a higher level of promotional sales activities, which adversely affected our profitability. We believe our comparable store sales results in fiscal 2002 and the first half of 2003 also reflected in large part customer dissatisfaction with our product offerings. When our new management took over in January 2003, they initiated a program to upgrade the quality and style of our merchandise

assortments. These changes were not implemented until our Fall and Holiday 2003 product offerings. We believe that our comparable store sales increase in fiscal 2004 reflects a positive customer response to our merchandise development efforts and an emphasis on customer service in our retail stores.

An important aspect of our business strategy has been an expansion program designed to reach new and existing customers through the opening of new stores. However, as a result of an overall slowdown in the economic environment in 2002 and our declining comparable store sales trends in 2002 and 2003, we curtailed in the number of new store openings to concentrate on improving the store productivity (as measured by sales per square foot) of our existing stores. We believe that we have begun to accomplish this, which is reflected in the increase in our store productivity as sales per square foot increased to \$397 in 2004 from \$337 per square foot in 2003. We opened five new stores (and closed 4 stores) in fiscal 2004 and expect to accelerate the pace of our store openings in fiscal 2005 with the addition of ten new stores.

Results of Operations

Our consolidated statements of operations presented as a percentage of revenues are as follows:

	Fiscal Year Ended		
	January 29, 2005	January 31, 2004	February 1, 2003
Revenues(1)	100.0%	100.0%	100.0%
Cost of goods sold, including buying and occupancy costs(2)	59.5	63.8	61.5
Gross profit(2)	40.5	36.2	38.5
Selling, general and administrative expenses(2)	35.8	40.7	39.3
Income/(loss) from operations	4.7	(4.5)	(0.7)
Interest expense, net	10.9	9.3	5.3
(Gain) loss on refinancing of debt	6.2	(6.0)	—
Insurance proceeds	—	(.6)	(0.2)
Loss before income taxes	(12.4)	(7.2)	(5.8)
Provision (benefit) for income taxes	0.1	0.1	(0.5)
Net loss	(12.5)%	(7.3)%	(5.3)%

Selected retail store data:

Number of stores open	197	196	194
Sales per gross square foot	\$ 397	\$ 337	\$ 351
Comparable store sales change	16.4 %	(2.5)%	(11.2)%

(1) Includes licensing, shipping and handling fees and other.

(2) Our gross margins may not be comparable to others, as some companies include all of the costs related to their distribution network in cost of goods sold while others, like us, exclude all or a portion of them from gross margin and include them in selling, general and administrative expenses.

Fiscal 2004 Compared to Fiscal 2003

Net Sales

Net sales in fiscal 2004 increased by \$114.2 million, or 16.6%, to \$804.2 million from \$690.0 million in fiscal 2003. The increase resulted primarily from an increase in J.Crew Retail sales of \$92.6 million, due to an increase of 16.4% in comparable store sales, and an increase in J.Crew Direct sales of \$25.1 million, or 14%, which we believe resulted in part from a 40% increase in the second half of 2004 in the number of styles presented in our catalog and on our website, as well as the mailing of four new catalog editions. These increases were offset in part by a decrease in other revenues of \$3.5 million resulting primarily from a decrease in shipping and handling fees as a result of a decline in orders in the J.Crew Direct business in the first half of fiscal 2004. We believe that the increase in comparable store sales and in the J. Crew Direct business resulted from the positive customer response to the continuing improvements in our product offerings and an emphasis on customer service.

Gross Profit

Gross profit increased by \$75.7 million, or 30.3%, to \$325.4 million in fiscal 2004 from \$249.7 million in fiscal 2003. Gross margin increased from 36.2% in 2003 to 40.5% in 2004, attributable primarily to a 440 basis point increase in merchandise margins, which resulted from lower markdowns and improved inventory management in 2004, coupled with the negative effect on 2003 margins from the liquidation of prior season inventories in the first half of the year.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased by \$7.2 million, or 2.6%, to \$287.7 million in fiscal 2004 from \$280.5 million in fiscal 2003. The increase resulted primarily from increases in variable store operating expenses and incentive compensation. These increases were offset in part by a decrease in depreciation and amortization of \$6.0 million related primarily to computer equipment, and a decrease in catalog selling costs of \$3.7 million due primarily to a reduction in pages circulated from 5.8 billion to 5.4 billion. As a percentage of sales, selling, general and administrative expenses decreased from 40.7% in 2003 to 35.8% in 2004, resulting primarily from an increase in operating leverage due to the increase in revenues.

Interest Expense

Interest expense for Group increased by \$23.8 million to \$87.6 million in fiscal 2004 from \$63.8 million in fiscal 2003. The increase resulted primarily from the inclusion as interest of dividends on mandatorily redeemable preferred stock for the full year in 2004 as compared to the inclusion only in the second half of fiscal 2003, which resulted in an increase of \$18.9 million. There were also increases in interest of \$8.0 million, including amortization of debt issuance discount related to the 16% Senior Discount Contingent Principal Notes due 2008 issued in May 2003 and \$2.7 million on the 9³/₄% Senior Subordinated Notes due 2014 issued in December 2004. These increases were offset by a reduction of \$4.4 million of interest on the 13¹/₈% Senior Discount Debentures due to the exchange offer completed in May 2003 and \$1.5 million reduction on the 10³/₈% Senior Subordinated Notes due 2007 due to their redemption in December 2004.

Interest expense for Operating increased by \$1.1 million to \$21.6 million in fiscal 2004 from \$20.5 million in fiscal 2003. The increase was primarily due to \$2.7 million of interest on \$275 million of the 9³/₄% Senior Subordinated Notes issued in December 2004, offset in part by \$1.6 million of interest on the 10³/₈% Senior Subordinated Notes that were redeemed in such transaction.

Gain (loss) on Refinancing of Debt

The gain (loss) on refinancing of debt was a loss of \$49.8 million in fiscal 2004 compared to a gain of \$41.1 million in 2003. In the fourth quarter of 2004, we redeemed \$150.0 million of 10³/₈% Senior Subordinated Notes and \$169.0 million outstanding amount of 16% Senior Discount Contingent Principal Notes. The funds used to redeem these notes were provided by the issuance of \$275 million in new term loans and internally available funds. These term loans were subsequently converted into equivalent new 9³/₄% Senior Subordinated Notes due 2014 of Operating.

This debt refinancing resulted in a loss of \$49.8 million at Group in 2004 consisting of (a) redemption premiums of \$15.3 million, (b) the write-off of deferred financing costs related to the old debt of \$3.2 million, and (c) the write-off of unamortized debt issuance costs of \$31.3 related to the 16% Senior Discount Contingent Principal Notes. The loss on refinancing of debt at Operating in fiscal 2004 was \$4.0 million consisting of redemption premiums of \$2.6 million and the write-off of deferred financing costs of \$1.4 million.

The gain of \$41.1 million in fiscal 2003 resulted from the issuance of the 16% Senior Discount Contingent Principal Notes in May 2003.

Insurance Proceeds

Insurance proceeds of \$3.8 million in fiscal 2003 and \$1.8 million in fiscal 2002 represent recoveries for claims related to the destruction of our World Trade Center store on September 11, 2001. The recovery in fiscal 2003 is the final settlement of this claim.

Income Taxes

Group files a consolidated federal tax return, which includes all its wholly owned subsidiaries. Each subsidiary files separate state tax returns in the required jurisdictions. Group and its subsidiaries have entered into a tax sharing agreement providing (among other things) that each of the subsidiaries will reimburse Group for its share of income taxes based on the proportion of such subsidiaries' tax liability on a separate return basis to the total tax liability of Group. Accordingly, the following discussion pertains to Group.

In fiscal 2002, we established a valuation allowance of \$21.0 million to reduce the net deferred tax assets to the estimated recoverable amount at February 1, 2003. The valuation allowance was offset by a \$9.0 million benefit from the reversal of prior year tax accruals. The valuation allowance was recorded in fiscal 2002 as a result of the significance of our net loss in fiscal 2002 and management's projection of taxable income/loss in the near future. Management had previously concluded that considering all factors, including available tax planning strategies and projections of future taxable income, it was more likely than not that the net deferred income tax assets would be realized. However, considering our substantially increased losses and declining trends and projections of operating losses in the near future, the fact that our operating results for fiscal 2002 were significantly worse than originally forecasted and the downward revision of the outlook for fiscal year 2003 and forward, we reassessed the need for a valuation allowance. We believed in fiscal 2002 that the "positive evidence" no longer outweighed the "negative evidence" and a valuation allowance was, therefore, necessary. The tax accruals were reversed in 2002 based on a proposed IRS settlement of open years and the results of state audits at amounts less than amounts accrued. An additional valuation allowance of \$5.0 million was recorded in fiscal 2003 to fully reserve the net deferred tax assets at January 31, 2004. This increase was offset by additional tax refunds and a reduction in prior year tax accruals as a result of the finalization of certain tax audits. The Company did not recognize any tax benefits in fiscal 2004 and does not expect to recognize any tax benefits in future operations until an appropriate level of profitability is sustained.

Fiscal 2004, 2003 and 2002 include state and foreign tax provisions of \$0.6 million, \$0.5 million and \$0.4 million, respectively.

Net Loss

The net loss of Group in fiscal 2004 was \$100.3 million compared to \$50.2 million in fiscal 2003. The loss in fiscal 2004 includes a loss on the refinancing of debt of \$49.8 million while fiscal 2003 included a gain on exchange of debt of \$41.1 million and insurance proceeds of \$3.8 million. Excluding these items, the net loss for Group for fiscal 2004 would have been \$50.5 million compared to a net loss of \$95.1 million last year. The improvement in fiscal 2004 results is due primarily to the 16.6% increase in net sales and the improvement in gross margin. Operating had net income of \$11.4 million in fiscal 2004 compared to a net loss of \$42.0 million in fiscal 2003, an improvement of \$53.4 million.

Fiscal 2003 Compared to Fiscal 2002

Net Sales

Net sales in fiscal 2003 decreased by \$78.3 million, or 10.2%, to \$690.0 million from \$768.3 million in fiscal 2002. The decrease resulted primarily from a decrease in J.Crew Direct sales of \$74.5 million, or 30%, resulting from (a) 25% decrease in catalog circulation from 7.8 billion pages in 2002 to 5.8 billion pages in 2003 including the elimination of women's only and clearance catalogs in the second half of the year, (b) a decrease in density (items per page) resulting from a 30% reduction in style

counts, and (c) a reduction in promotional practices, including promotional e-mails. Other revenues decreased by \$6.6 million resulting primarily from a decrease in shipping and handling fees as a result of a decline in orders in Direct. These decreases were offset in part by an increase of \$2.8 million in J.Crew Retail sales. A decline of 2.5% in comparable store sales was offset by sales from four stores opened in fiscal 2003 and 16 stores opened in 2002 that were open for a full year in fiscal 2003. We believe that the improvement in comparable store sales performance in 2003 was the result of an improving economy and an upgrade in the quality and style of our merchandise assortments in the second half of the year.

Gross Profit

Gross profit decreased by \$46.4 million, or 15.7%, to \$249.7 million from \$296.1 million. Gross margin decreased from 38.5% to 36.2%, attributable primarily to a 160 basis point increase in buying and occupancy costs as a percentage of revenues resulting from the spreading of fixed buying and occupancy costs over a lower revenue base, and a decrease of 70 basis points in merchandise margins primarily from the liquidation of prior season's inventories in the first half of 2003.

Selling, General and Administrative Expenses

Selling, general and administrative expenses decreased by \$21.2 million, or 7.0%, to \$280.5 million from \$301.7 million. The decrease resulted primarily from lower catalog selling costs of \$13.2 million related primarily to the reduction in pages circulated, including the elimination of women's only editions and clearance catalogs in the second half of 2003, as well as a decrease in severance and other one-time employment-related charges of \$10.0 million. These decreases were offset in part by increased store expenses resulting from additional stores in operation in 2003. As a percentage of sales, selling, general and administrative expenses increased from 39.3% to 40.7%, resulting primarily from the spreading of fixed overhead expenses over a lower revenue base.

Interest Expense

Interest expense for Group increased by \$22.8 million to \$63.8 million from \$41.0 million. The increase resulted from (a) the inclusion as interest of \$14.2 million of dividends on mandatorily redeemable preferred stock which classification as interest expense commenced in the third quarter of 2003, and (b) interest on the 16% Senior Discount Contingent Principal Notes of \$21.9 million, including amortization of debt issuance discount, issued in the exchange offer completed in May 2003. These increases were offset by a reduction of \$10.4 million of interest on the 13¹/₈% Senior Discount Debentures that were exchanged for the 16% Senior Discount Contingent Principal Notes, and lower deferred financing costs which resulted primarily from a write off of \$1.8 million related to the refinancing of our working capital credit facility in fiscal 2002.

Interest expense for Operating decreased by \$2.7 million to \$20.5 million from \$23.2 million. The decrease was primarily attributable to a reduction in amortization of deferred financing costs, which resulted primarily from a write off of \$1.8 million related to the refinancing of our working capital credit facility in fiscal 2002.

Gain on Refinancing of Debt

The net gain on exchange of debt of \$41.1 million in 2003 reflects the difference between the fair value of the 16% Senior Discount Contingent Principal Notes at date of issuance and the carrying value of the 13¹/₈% Senior Discount Debentures of \$44.1 million less related expenses which consist of (a) the additional expense of 2⁷/₈% from October 15, 2002 to May 6, 2003 paid to the note holders who accepted the exchange offer completed in May 2003 (\$1.9 million) and (b) the write off of unamortized deferred financing costs related to the debentures exchanged in the May 2003 exchange offer (\$1.1 million).

Insurance Proceeds

For the discussion of insurance proceeds, see "Fiscal 2004 compared to Fiscal 2003—Insurance Proceeds."

Income Taxes

For the discussion of income taxes, see "Fiscal 2004 Compared to Fiscal 2003—Income Taxes".

Net Loss

The net loss of Group for fiscal 2003 was \$50.2 million compared to a net loss of \$40.6 million in fiscal 2002. However, the results in fiscal 2003 included a gain on the exchange of debt of \$41.1 million and an increase in insurance proceeds of \$2.0 million. Excluding these items, the net loss of Group for fiscal 2003 would have been \$95.1 million, an increase of \$52.7 million from the prior year. This increase in net loss is primarily attributed to the decrease in gross profit in fiscal 2003, attributable to the sales decline and the increase in interest expense.

The net loss of Operating increased to \$42.0 million in fiscal 2003 from \$8.8 million in fiscal 2002. This increase resulted primarily from the decrease in gross profit resulting from the sales decline.

Liquidity and Capital Resources

Our sources of liquidity are primarily cash flows from operations and borrowings under our working capital credit facility. Our primary cash needs are for capital expenditures incurred primarily for opening new stores and system enhancements, debt service requirements and working capital.

On November 21, 2004, Operating entered into a Senior Subordinated Loan Agreement with entities managed by Black Canyon Capital LLC and Canyon Capital Advisors LLC, which provided for a term loan of \$275.0 million. The proceeds of the term loan were used to redeem in full Operating's outstanding 10³/₈% Senior Subordinated Notes due 2007 (\$150.0 million) and to redeem, in part, Intermediate's 16% Senior Discount Contingent Principal Notes due 2008 (\$125.0 million). In January 2005, we redeemed the remaining \$44 million of outstanding 16% Senior Discount Contingent Principal Notes using internally available funds. On March 18, 2005, the term loan was converted into equivalent new 9³/₄% Senior Subordinated Notes of Operating due 2014 in accordance with the terms of the loan agreement. This refinancing will generate approximately \$16.0 million of annual interest savings.

On December 23, 2004, Operating entered into an Amended and Restated Loan and Security Agreement, which we refer to as the Amended Wachovia Credit Facility, with Wachovia Capital Markets LLC, as arranger, Wachovia Bank National Association, as administrative agent, Bank of America N.A., as syndication agent, Congress Financial Corporation, as collateral agent, and a syndicate of lenders, which provides for maximum credit availability of up to \$170.0 million (which can be increased to \$250.0 million if certain conditions are met). The Amended Wachovia Credit Facility provides for revolving loans and letters of credit of up to \$170.0 million and expires in December 2009. The total amount of availability is limited to the sum of invested cash, 90% of eligible receivables, 95% of the net recovery percentage of inventories (as determined by inventory appraisal) for the period of August 1 through December 15, 92.5% of the net recovery percentage of inventories for the period December 16 through July 31 and real estate availability of 65% of appraised fair market value. As of January 29, 2005, there was \$27.0 million of excess availability under the Amended Wachovia Credit Facility.

The Amended Wachovia Credit Facility includes restrictions, including the incurrence of additional indebtedness, the payment of dividends and other distributions, the making of investments, the granting of loans and the making of capital expenditures. We are required to maintain a minimum of fixed interest charge coverage of 1.1 if excess availability is less than \$20.0 million for any 30 consecutive day

period. We have at all times been in compliance with all financial covenants under the Amended Wachovia Credit Facility.

The Amended Wachovia Credit Facility permits restricted payments (by way of dividends or other distributions) with respect to, among other things, our capital stock payable solely in additional shares of our capital stock, our tax sharing agreement, the Series A preferred stock of Group, the Series B preferred stock of Group and the 13¹/₈% Senior Discount Debentures due 2008 of Group. Our ability to declare dividends on our capital stock is also limited by Delaware law, which permits a company to pay dividends on its capital stock only out of its surplus or, in the event that it has no surplus, out of its net profits for the year in which a dividend is declared or for the immediately preceding fiscal year. Under the Amended Wachovia Credit Facility, the assets of Operating and its subsidiaries are restricted.

Cash provided by operating activities was \$58.8 million in fiscal 2004, \$18.2 million in fiscal 2003 and \$31.8 million in fiscal 2002. The increase in 2004 resulted from the significant increase in operating income. Cash provided in 2003 and 2002 resulted from improvements in working capital, due primarily to reductions in inventories of \$41.3 million in 2003 and \$31.6 million in 2002, which offset the operating losses in those years.

Capital expenditures were \$13.4 million in fiscal 2004, \$9.9 million in fiscal 2003 and \$26.9 million in fiscal 2002. Capital expenditures related to new stores were \$5.9 million, \$5.7 million and \$17.2 million during the three years. Anticipated capital expenditures in fiscal 2005 are approximately \$25 million, primarily for 10 new stores and information technology initiatives.

There were no borrowings under our working capital credit facility at January 29, 2005 and January 31, 2004. Average borrowings under the credit facility were none in fiscal 2004, \$1.0 million in fiscal 2003 and \$40.4 million in fiscal 2002. Long-term indebtedness increased by \$25.8 million in fiscal 2003 consisting of \$20.0 million of TPG-MD Investment LLC notes payable due in 2008 and \$5.8 million under the our working capital credit facility, which was paid off in January 2005.

Management believes that its current cash position, cash flow from operations and availability under the Amended Wachovia Credit Facility will provide adequate funds for our foreseeable working capital needs, planned capital expenditures and debt service obligations. Our ability to fund our operations and make planned capital expenditures, to make scheduled debt payments, to refinance indebtedness and to remain in compliance with the financial covenants under our debt agreements depends on our future operating performance and cash flow, which in turn, are subject to prevailing economic conditions and to financial, business and other factors, some of which are beyond our control.

Restatement

The consolidated statements of cash flows for Group and Operating for the years ended January 31, 2004 and February 1, 2003 have been restated to reclassify the proceeds from construction allowances from a reduction of capital expenditures in cash flows from investing activities to an increase in cash flow from operating activities. There was no effect on the Company's consolidated balance sheet or consolidated statement of operations.

Off Balance Sheet Arrangements

We enter into letters of credit to facilitate the international purchase of merchandise. Standby letters of credit are required to secure certain of our obligations, including insurance programs and duties related to import purchases.

Letters of Credit	Within 1 Year	2-3 Years	4-5 Years	After 5 Years	Total
Standby	\$ 0.7	\$ —	\$ —	\$ 5.0	\$ 5.7
Import	53.0	—	—	—	53.0
	<u>\$ 53.7</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 5.0</u>	<u>\$ 58.7</u>

Contractual Obligations

The following summarizes our contractual obligations as of January 29, 2005 and the effect such obligations are expected to have on our liquidity and cash flows in future periods.

	Within 1 Year	2-3 Years	4-5 Years	After 5 Years	Total
	(\$ in millions)				
Long-term debt obligations	\$ —	\$ —	\$ 43.7	\$ 275.0	\$ 318.7
Redeemable preferred stock	—	—	258.3	—	258.3
Operating lease obligations(1)	54.3	99.3	81.0	98.8	333.4
Purchase obligations					
Inventory commitments	197.7	—	—	—	197.7
Other	5.7	8.0	—	—	13.7
Employment agreements	1.9	3.8	—	—	5.7
	205.3	11.8	—	—	217.1
Total	\$ 259.6	\$ 111.1	\$ 383.0	\$ 373.8	\$ 1,127.5

- (1) Operating lease obligations represent obligations under various long-term operating leases entered in the normal course of business for retail and factory stores, warehouses, office space and equipment requiring minimum annual rentals. Operating lease expense is a significant component of our operating expenses. The lease terms range for various periods of time in various rental markets and are entered into at different times, which mitigates exposure to market changes which could have a material effect on the Company's results of operations within any given year.

Impact of Inflation

Our results of operations and financial condition are presented based upon historical cost. While it is difficult to accurately measure the impact of inflation due to the imprecise nature of the estimates required, we believe that the effects of inflation, if any, on our results of operations and financial condition have been minor. However, there can be no assurance that during a period of significant inflation, our results of operations would not be adversely affected.

Seasonality

We experience two distinct selling seasons, spring comprised of the first and second fiscal quarters and fall comprised of the third and fourth fiscal quarters. Net sales are usually substantially higher in the fall season and selling, general and administrative expenses as a percentage of net sales are usually higher in the spring season. Approximately 33% of annual net sales in fiscal 2004 occurred in the fourth fiscal quarter. Our working capital requirements also fluctuate throughout the year, increasing substantially in September and October in anticipation of the holiday season inventory requirements.

Recent Accounting Pronouncements

In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. FIN 46R applies to variable interests in variable interest entities created after December 31, 2003. For variable interests in variable interest entities created before January 1, 2004, the Interpretation applies beginning on January 1, 2005. For any variable interest entities that must be consolidated under FIN 46R that were created before January 1, 2004, the assets, liabilities and noncontrolling interests of the variable interest entity initially would be

measured at their carrying amounts with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting change. If determining the carrying amounts is not practicable, fair value at the date FIN 46R first applies may be used to measure the assets, liabilities and noncontrolling interest of the variable interest entity. The adoption of FIN 46R did not have any effect on the financial statements taken as a whole as of January 29, 2005, and for the year then ended.

In December 2004, the FASB issued Statement No. 123 R, Share-Based Payment. This revision to Statement No. 123 requires that compensation expense be recognized for the fair value of stock options over their vesting period and changes the method of expense recognition for performance-based stock awards. The Statement is required to be adopted by the Company for fiscal years beginning after December 15, 2005 and applies to all outstanding stock options and stock awards that have not yet vested at the date of adoption. Management is evaluating the effects of this Statement.

Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations is based upon the consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. We base our estimates on historical experience and other assumptions that are believed to be reasonable under the circumstances and evaluate these estimates on an on-going basis. Actual results may differ from these estimates under different assumptions or conditions.

The following critical accounting policies, which we have discussed with our audit committee, reflect the more significant estimates and judgments used in the preparation of our consolidated financial statements. We do not believe that changes in these assumptions and estimates are likely to have a material impact on our consolidated financial statements.

Inventory Valuation

Merchandise inventories are carried at the lower of cost or market. We evaluate all of our inventories to determine excess inventories based on estimated future sales. Excess inventories may be disposed of through our factory channel, internet clearance sales and other liquidations. Based on historical results experienced through various methods of disposition, we write down the carrying value of inventories that are not expected to be sold at or above costs.

Deferred Catalog Costs

The costs associated with direct response advertising, which consist primarily of catalog production and mailing costs, are capitalized and amortized over the expected future revenue stream of the catalog mailings, which approximates four months. The expected future revenue stream is determined based on historical revenue trends developed over an extended period of time. If the current revenue streams were to diverge from the expected trend, our future revenue streams would be adjusted accordingly.

Asset Impairment

We are exposed to potential impairment if the book value of our assets exceeds their future cash flows. The major components of our long-lived assets are store fixtures, equipment and leasehold improvements. The impairment of unamortized costs is measured at the store level and the unamortized cost is reduced to fair value if it is determined that the sum of expected future net cash flows is less than net book value.

Sales Returns

We must make estimates of future sales returns related to current period sales. Management analyzes historical returns, current economic trends and changes in customer acceptance of our products when evaluating the adequacy of the reserve for sales returns.

Income Taxes

We have significant deferred tax assets resulting from net operating loss carryforwards and temporary differences, which will reduce taxable income in future periods. Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes" states that a valuation allowance is required when it is more likely than not that all or a portion of a deferred tax asset will not be realized. A review of all available positive and negative evidence needs to be considered, including a company's current and past performance, the market environment in which a company operates, length of carryback and carryforward periods, existing contracts or sales backlog that will result in future profits, etc. Forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years. Cumulative losses weigh heavily in the overall assessment. As a result of our assessments, we established a valuation allowance to reduce our net deferred tax assets to their estimated realizable value of \$5.0 million at February 1, 2003 and we provided additional allowances at January 31, 2004 and January 29, 2005 to fully reserve our net deferred tax assets. We do not expect to recognize any tax benefit in future results of operations until an appropriate level of profitability is sustained.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our principal market risk relates to interest rate sensitivity, which is the risk that future changes in interest rates will reduce our net income or net assets. Our variable rate debt consists of borrowings under the Amended Wachovia Credit Facility. The interest rates are a function of the bank prime rate or LIBOR. A one percentage point increase in the base interest rate would result in approximately \$100,000 change in income before taxes for each \$10 million of borrowings.

We have a licensing agreement in Japan that provides for royalty payments based on sales of J.Crew merchandise as denominated in yen. We have entered into forward foreign exchange contracts from time to time in order to minimize this risk. At January 29, 2005, there were no forward foreign exchange contracts outstanding.

We also enter into letters of credit to facilitate the international purchase of merchandise. The letters of credit are primarily denominated in U.S. dollars. Outstanding letters of credit at January 29, 2005 were \$58.7 million, including \$5.7 million of standby letters of credit.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Financial Statements are set forth herein commencing on page F-1 of this Report.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

With the participation of the Company's management, including the Chief Executive Officer and the Chief Financial Officer, the Company has conducted an evaluation of its disclosure controls and procedures as of the end of the period covered by this report. Such evaluation included a review of the facts and circumstances relating to the correction of certain of the Company's lease accounting

practices. As a result of the February 7, 2005 letter issued by the Office of the Chief Accountant of the Securities and Exchange Commission to the American Institute of Certified Public Accountants, the Company concluded that certain of its previously established lease accounting practices were not appropriate and determined to restate its Consolidated Statements of Cash Flows for prior years to report construction allowances as operating activities, rather than investing activities. There was no impact on net income as a result of the changes. Based solely on this change in lease accounting practices, the Company's Chief Executive Officer and the Chief Financial Officer have concluded that the Company's disclosure controls and procedures were not effective as of the end of the period covered by this report.

Such officers also confirm that there were no significant changes in the Company's internal controls over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART III

Information required by items 10-14 with respect to Operating has been omitted pursuant to General Instruction I of Form 10-K. Information required by items 10-14 with respect to Group is described below.

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The following table sets forth the name, age and position of individuals who are serving as directors and executive officers of Group as of April 1, 2005.

Name	Age	Position
Millard Drexler	60	Chief Executive Officer, Chairman of the Board and Director
Jeffrey Pfeifle	46	President
Roxane Al-Fayez	48	Executive Vice President, Catalog & e-Commerce
Amanda Bokman	41	Executive Vice President, Chief Financial Officer
Tracy Gardner	41	Executive Vice President, Merchandising, Planning & Production
Scott Hyatt	47	Senior Vice President, Manufacturing
Nicholas Lamberti	62	Vice President, Corporate Controller
Richard Boyce	50	Director
Jonathan Coslet	40	Director
James Coulter	45	Director
Steven Grand-Jean	62	Director
Thomas Scott	39	Director
Stuart Sloan	61	Director
Josh Weston	76	Director
Emily Woods	43	Director

Millard Drexler. Mr. Drexler became Chief Executive Officer in January 2003 and Chairman of the Board and a Director in March 2003. Before joining the Company, Mr. Drexler was Chief Executive Officer of The Gap, Inc. from 1995 until September 2002, and prior thereto he was President of The Gap, Inc. since 1987. Mr. Drexler also serves on the Board of Directors of Apple Computer Inc.

Jeffrey Pfeifle. Mr. Pfeifle became President in February 2003. Before joining the Company, Mr. Pfeifle was Executive Vice President, Product and Design of the Old Navy division of The Gap, Inc. from 1995.

Roxane Al-Fayez. Ms. Al-Fayez became Executive Vice President, Catalog & e-Commerce in October 2003. Before joining the Company, she was Vice President of Operations, Gap, Inc. Direct for six years.

Amanda Bokman. Ms. Bokman became Executive Vice-President and Chief Financial Officer in May 2004. Before joining the Company, Ms. Bokman was Senior Vice-President and Chief Financial Officer of one of the four major segments of Jones Apparel Group, Inc. from 2001 and Vice-President and Chief Financial Officer of McNaughton Apparel Group, Inc. for nine years prior thereto.

Tracy Gardner. Ms. Gardner became Executive Vice President, Merchandising, Planning & Production in March 2004. Prior to joining the Company, Ms. Gardner held various positions at The Gap, Inc., including Senior Vice President of Adult Merchandising for GAP brand from 2002 to March 2004, Vice-President of Womens' Merchandising for the Banana Republic division from 2001 to 2002, Vice-President of Mens' Merchandising for the Banana Republic division from 1999 to 2001, and Divisional Merchandising Manager of Mens' Wovens for the Banana Republic division prior to 1999.

Scott Hyatt. Mr. Hyatt has been Senior Vice President, Manufacturing since 1998. Before joining the Company, Mr. Hyatt was Vice President, Production and Sourcing of the Express division of Limited Brands, a retail apparel company, from 1996 to 1998.

Nicholas Lamberti. Mr. Lamberti has been Vice President, Corporate Controller for more than five years. Mr. Lamberti also served as acting Chief Financial Officer from August 2003 until Ms. Bokman joined the Company in May 2004.

Richard Boyce. Mr. Boyce has been a Director since 1997 and has periodically served as Chief Executive Officer between 1997 and 1999 while also providing operating oversight to the remainder of the Texas Pacific Group portfolio. Mr. Boyce is a Senior Operating Partner of Texas Pacific Group and joined Texas Pacific Group in 1997. Mr. Boyce is also the Chairman of the Executive Committee of the Board of Directors of Burger King Corporation and a Director of ON Semiconductor Corporation, Spirit Group, Ltd. and Kraton Polymers.

Jonathan Coslet. Mr. Coslet became a Director in 2003. Mr. Coslet is a senior Partner of Texas Pacific Group and is responsible for the investment firm's generalist and healthcare investment activities. Prior to joining Texas Pacific Group, Mr. Coslet worked in the investment banking department of Donaldson, Lufkin & Jenrette, specializing in leveraged acquisitions and high yield finance from 1991 to 1993. Mr. Coslet also serves on the Board of Directors of Burger King Corporation, Petco Animal Supplies, Inc., Quintiles Transnational Corp., IASIS Healthcare Corp. and Fidelity National Information Services.

James Coulter. Mr. Coulter has been a Director since 1997. Mr. Coulter is a founding Partner of Texas Pacific Group, and has been Managing General Partner of Texas Pacific Group for more than eight years. Mr. Coulter also serves on the Board of Directors of Conexant Systems, Inc., Seagate Technology, Inc. and Zhone Technologies.

Steven Grand-Jean. Mr. Grand-Jean became a Director in 2003. Mr. Grand-Jean has been President of Grand-Jean Capital Management for more than five years.

Thomas Scott. Mr. Scott has been a Director since 2002. Mr. Scott is a founding partner of Plum TV, LLC, a television station network in select resort markets, and has served as its Chief Executive Officer and Executive Co-Chairman since September 2003. He is also a founding partner of Nantucket Allserve Inc., a beverage supplier, and has served as Co-Chairman thereof since 1989 and Co-Chairman and Co-Chief Executive Officer from 1989 to 2000. Mr. Scott has also served as Co-Chairman of Shelflink, a supply chain software company, since 2000. Mr. Scott is married to Emily Woods, a Director of the Company.

Stuart Sloan. Mr. Sloan has been a Director since September 2003. Mr. Sloan is the founder of Sloan Capital Companies, a private investment company, and has been a Principal thereof since 1984. Mr. Sloan also serves on the Board of Directors of Anixter International, Inc. and Rite Aid Corp.

Josh Weston. Mr. Weston has been a Director since 1998. Mr. Weston has also served as Honorary Chairman of the Board of Directors of Automatic Data Processing, a computing services business, since 1998. Mr. Weston was Chairman of the Board of Automatic Data Processing from 1996 until 1998, and Chairman and Chief Executive Officer for more than five years prior thereto. Mr. Weston also serves on the Board of Directors of Gentiva Health Services, Inc. and Russ Berrie & Company, Inc.

Emily Woods. Ms. Woods served as Chairman of the Board of Directors of Group from 1997 to 2003, and continues to serve as a Director. Ms. Woods started work at the Company the year that it was founded in 1983 and has also previously served as its Chief Executive Officer and Vice Chairman. Ms. Woods is married to Thomas Scott, a Director of the Company.

Our Board of Directors

Our Board of Directors currently has 9 members. Directors serve until the next annual meeting of shareholders or until his or her successor has been elected and qualified. Directors may be removed at any time, with or without cause, by vote of our shareholders. Our Board of Directors currently has two standing committees—an Audit Committee and a Compensation Committee.

Audit Committee. The primary duties of the Audit Committee include assisting the Board of Directors in its oversight of (i) the integrity of our financial statements and financial reporting process; (ii) the integrity of our internal controls regarding finance, accounting and legal compliance; and (iii) the independence and performance of our independent auditors and internal audit function. The Committee also reviews our critical accounting policies, our annual and quarterly reports on Form 10-K and Form 10-Q, and our earnings releases before they are published. The Committee has sole authority to engage, evaluate and replace the independent auditor. The Committee also has the authority to retain special legal, accounting and other consultants it deems necessary in the performance of its duties. The Committee meets regularly with our management, independent auditors and internal auditors to discuss our internal controls and financial reporting process and also meets regularly with the independent auditors and internal auditors in private.

The current members of the Audit Committee are Messrs. Boyce, Grand-Jean and Weston (Chairperson). The Board of Directors has determined that Josh Weston qualifies as an "audit committee financial expert" and is independent under the applicable rules of the Securities and Exchange Commission.

Compensation Committee. The primary duty of the Compensation Committee is to discharge the responsibilities of the Board of Directors relating to compensation practices for our executive officers and other key employees, as the Committee may determine, to ensure that management's interests are aligned with the interests of our equity holders. The Committee also reviews and makes recommendations to the Board of Directors with respect to our employee benefits plans, compensation and equity-based plans and compensation of Directors. The current members of the Compensation Committee are Messrs. Coulter (Chairperson) and Sloan and Ms. Woods.

Compensation of Directors. Directors who are our employees or representatives of Texas Pacific Group (Messrs. Boyce, Coslet, Coulter and Drexler) do not receive any compensation for their services. All other Directors (Messrs. Grand-Jean, Scott, Sloan and Weston and Ms. Woods) received the following as compensation in 2004: (1) 5,000 shares of restricted Group common stock and (2) a non-qualified stock option to purchase 10,000 shares of Group common stock. In lieu of receiving such stock option, a Director could elect to have the Company make one or more charitable contributions on his or her behalf in a total amount up to \$50,000. Mr. Weston alone elected to have the Company make charitable contributions on his behalf of \$50,000. The restricted stock awards have a value based on the fair market value of the common stock on the effective grant date and vested immediately. The options have an exercise price of \$6.82 per share, have a term of 10 years and become exercisable and vest in two equal installments in December 2004 and December 2005. If a Director ceases to serve as a Director for any reason, other than removal for cause, any options vested at the time of termination of his or her services will remain exercisable for 90 days (but no longer than the 10 year term of the options).

Our Board of Directors has also approved the following to be paid as compensation to all eligible Directors for their services in 2005: (1) a cash retainer of \$30,000 and (2) a non-qualified stock option to purchase 10,000 shares of Group common stock. Upon grant, the options will have an exercise price to be determined at the time of grant, have a term of 10 years and become exercisable and vest in equal installments over a two year period. If a Director ceases to serve as a Director for any reason, other than removal for cause, any options vested at the time of termination of his or her services will

remain exercisable for 90 days (but no longer than the 10 year term of the options). In addition, the Chairman of the Audit Committee will receive additional cash compensation of \$10,000 for his services on such Committee. Directors who are our employees or representatives of Texas Pacific Group are not entitled to receive any compensation for their services.

Code of Ethics and Business Practices

We have a Code of Ethics and Business Practices that applies to all of our Directors and employees, including to our chief executive officer, chief financial officer, controller and our other senior financial officers. A copy of the Code is filed as an exhibit to this Annual Report on Form 10-K and is available free of charge upon written request to the Corporate Secretary, J.Crew Group, Inc., 770 Broadway, New York, NY 10003.

ITEM 11. EXECUTIVE COMPENSATION

The following table sets forth compensation paid by Group for fiscal 2004, 2003 and 2002:

- to our chief executive officer during fiscal 2004 and
- to each of the four other most highly compensated executive officers as of the end of fiscal 2004

						Long-Term Compensation		
		Annual Compensation			Awards	Payouts		
Name And Principal Position	Fiscal Year	Salary (\$)	Bonus (\$)	Other \$(l)	Restricted Stock Award(s)(a)	Numbers of Securities Underlying Options/SARS(a)	LTIP Payouts (\$)	All Other Compensation \$(b)
Millard Drexler Chief Executive Officer and Chairman	2004	200,000	—	484,500	(c)	25,000(d)	—	—
	2003	200,000	—	500,000	(c)	—	—	—
	2002	—	—	—	(c)	2,231,704	—	—
Jeffrey Pfeifle President	2004	760,000	500,000	—	(f)	—(g)	800,000	8,200
	2003	760,000	2,400,000(e)	—	(f)	—	400,000	—
	2002	—	—	—	(f)	390,548	—	—
Roxane Al-Fayez Executive Vice-President, Catalog & e-Commerce	2004	377,900	275,000(h)	83,800	(i)	10,000	—	1,700
	2003	115,400	100,000(h)		(i)	35,000	—	—
Tracy Gardner Executive Vice-President, Merchandising, Planning & Production	2004	398,100	450,000(j)	95,500	(k)	90,000	—	—
Scott Hyatt Senior Vice President, Manufacturing	2004	375,000	160,000	—	—	10,000	—	8,200
	2003	364,000	—	—	—	—	—	10,500
	2002	364,000	—	—	—	—	—	9,700

- (a) There is no established public market for shares of Group common stock. Holders of restricted stock have the same right to receive dividends as other holders of Group common stock. Group has not paid any cash dividends on its common stock. Based on customary corporate valuation techniques, including an analysis of the discounted value of Group's potential earnings and cash flow, the valuation of comparable companies and current book value per share, the value of a share of Group common stock was estimated to be less than \$1 as of January 1, 2003. The Company believes that the value is not materially different as of November 2004.

As of April 1, 2005, the named executive officers held the following aggregate number of restricted shares of Group common stock: Mr. Drexler—463,278 vested shares (of which 55,793 shares are held by a corporation of which Mr. Drexler is a principal) and 476,507 unvested shares; Mr. Pfeifle—80,900 vested shares and 105,898 unvested shares; Ms. Al-Fayez—6,250 vested shares and 28,750 unvested shares; Ms. Gardner—0 vested shares and 50,000 unvested shares. Mr. Hyatt did not hold any restricted shares of Group common stock.

- (b) All amounts represent contributions made by Group on behalf of the named executive officers to its 401(k) plan.
- (c) In November 2004, Mr. Drexler was granted 75,000 shares of Group common stock, of which 50% will vest on each of November 1, 2007 and November 1, 2008.

In September 2003, Mr. Drexler was granted 83,689 shares of Group common stock, of which 5,976 shares vested immediately upon grant, 19,429 shares vested on January 27, 2004, and 19,428 shares vested on January 27, 2005, and the remainder will vest in equal annual installments on January 27, 2006 and 2007.

In February 2003, Mr. Drexler was granted 725,303 shares of Group common stock, of which 181,326 shares vested on January 27, 2004 and 181,325 shares vested on January 27, 2005, and the remainder will vest in equal annual installments on January 27, 2006 and 2007. Mr. Drexler paid \$800,000 to Group for these shares, which was in excess of their fair market value at the time of grant. A corporation of which Mr. Drexler is a principal was also granted 55,793 shares of Group common stock, all of which vested immediately upon grant.

- (d) This does not include the grant of certain replacement stock options to Mr. Drexler in May 2004 following the surrender by Mr. Drexler of the same number of stock options in September 2003. We refer you to "Employment Agreements and Other Compensation Arrangements—Employment and Other Agreements" for information on the repricing of Mr. Drexler's premium stock options.
- (e) This amount represents a \$2,000,000 sign-on bonus and a \$400,000 guaranteed annual bonus for fiscal 2003.
- (f) In November 2004, Mr. Pfeifle was granted 25,000 shares of Group common stock, of which 50% will vest on each of November 1, 2007 and November 1, 2008.

In September 2003, Mr. Pfeifle was also granted 50,213 shares of Group common stock, of which 12,554 shares vested on February 1, 2004 and 12,553 shares vested on February 1, 2005, and the remainder will vest in equal annual installments on February 1, 2006 and 2007.

In February 2003, Mr. Pfeifle was granted 111,585 shares of Group common stock, of which 27,897 shares vested on February 1, 2004 and 27,896 shares vested on February 1, 2005, and the remainder will vest in equal annual installments on February 1, 2006 and 2007.

- (g) This does not include the grant of certain replacement stock options to Mr. Pfeifle in May 2004 following the surrender by Mr. Pfeifle of the same number of stock options in September 2003. We refer you to "Employment Agreements and Other Compensation Arrangements—Employment and Other Agreements" for information on the repricing of Mr. Pfeifle's premium stock options.
- (h) In fiscal 2004, this amount represents a \$25,000 one-time bonus paid in October 2004 and a \$250,000 annual bonus for fiscal 2004. In fiscal 2003, this amount represents a \$50,000 sign-on bonus and a \$50,000 guaranteed annual bonus for fiscal 2003.
- (i) In November 2004, Ms. Al-Fayez was also granted 10,000 shares of Group common stock, of which 50% will vest on each of November 1, 2007 and November 1, 2008.

In October 2003, Ms. Al-Fayez was granted 25,000 shares of Group common stock, of which 6,250 shares vested on October 22, 2004 and the remainder will vest in equal annual installments on October 22, 2005, 2006 and 2007.

- (j) This amount represents a \$150,000 sign-on bonus and \$300,000 annual bonus for fiscal 2004.
- (k) In May 2004, Ms. Gardner was granted 50,000 shares of Group common stock, which will vest in equal annual installments on April 1, 2006, 2007, 2008 and 2009.
- (l) We have reimbursed Mr. Drexler for our use for corporate business of a private aircraft owned by a company of which Mr. Drexler is a principal. The total reimbursements paid for our use of the aircraft in fiscal 2004 was approximately \$225,600. The total reimbursements paid for our use for corporate business of the aircraft and certain third party aircraft charters in fiscal 2003, which was not assessed and paid until 2004, was approximately \$49,300. All other amounts represent the reimbursement of certain business expenses to Mr. Drexler in accordance with the terms of his services agreement.

For Ms. Al-Fayez and Ms. Gardner, this includes \$83,800 in housing allowances and commuting reimbursements and \$95,500 in relocation compensation, respectively, in fiscal 2004. These include applicable tax gross-up amounts.

Option Grants in Last Fiscal Year

The following table shows information concerning stock options to purchase shares of Group common stock granted to any of the named executive officers during fiscal 2004.

Name	Individual Grants				Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term(b)	
	Number of Securities Underlying Options Granted(a)	Percent of Total Options Granted to Employees in Fiscal Year(a)	Exercise Price (\$/Sh)	Expiration Date	5% (\$)	10% (\$)
Millard Drexler	25,000	4%	\$ 6.82	2014	0(b)	0(b)
Roxane Al-Fayez	10,000	2%	\$ 6.82	2014	0(b)	0(b)
Tracy Gardner	50,000	9%	\$ 6.82	2014	0(b)	0(b)
Scott Hyatt	10,000	2%	\$ 6.82	2014	0(b)	0(b)
Jeffrey Pfeifle	—	—	—	—	—	—

- (a) Group has not granted any SARs. In addition, these figures do not reflect the grants of certain replacement stock options to Messrs. Drexler and Pfeifle in May 2004 following the surrender by them of the same number of stock options in September 2003. We refer you to "Employment Agreements and Other Compensation Arrangements—Employment and Other Agreements" for information on the repricing of Messrs. Drexler and Pfeifle's stock options.
- (b) There is no established public market for shares of Group common stock. Based on customary corporate valuation techniques, including an analysis of the discounted value of Group's potential earnings and cash flow, the valuation of comparable companies and current book value per share, the value of a share of Group common stock was estimated to be less than \$1 as of January 1, 2003. The Company believes that the value not materially different as of November 2004. As such, all outstanding options had exercise prices that exceeded the value of the stock as of such date, and the potential realizable value and value of unexercised in-the-money options is shown as zero.

Aggregated Option Exercises in Last Fiscal Year and Fiscal Year End Option Values

The following table shows the number of stock options held to purchase shares of Group common stock by the named executive officers of Group at the end of fiscal 2004. The named executive officers did not exercise any stock options in fiscal 2004.

Name	Shares Acquired on Exercise(#)	Value Realized(#)	Number of Securities Underlying Unexercised Options at Fiscal Year End Exercisable/Unexercisable	Value of Unexercised In-the-Money Options at Fiscal Year End\$(a) Exercisable/Unexercisable
Millard Drexler(b)	0		557,928/1,698,776	0/0
Roxane Al-Fayez	0		8,750/36,250	0/0
Tracy Gardner	0		0/90,000	0/0
Scott Hyatt	0		31,000/14,000	0/0
Jeffrey Pfeifle(b)	0		0/390,548	0/0

- (a) There is no established public market for shares of Group common stock. Based on customary corporate valuation techniques, including an analysis of the discounted value of Group's potential earnings and cash flow, the valuation of comparable companies and current book value per share, the value of a share of Group common stock was estimated to be less than \$1 as of January 1, 2003. The Company believes that the value is not materially different as of November 2004. As such, all outstanding options had exercise prices that exceeded the value of the stock as of such date, and the potential realizable value and value of unexercised in-the-money options is shown as zero.
- (b) On February 1, 2005, Mr. Pfeifle also vested in options to purchase 97,639 shares of Group common stock. In addition, we refer you to "Employment Agreements and other Compensation Arrangements—Employment and Other Agreements" for information on the grant of certain replacement stock options to Messrs. Drexler and Pfeifle in May 2004 following the surrender by them of the same number of stock options in September 2003.

Long Term Incentive Plan

The following table shows the eligibility of our President to receive long-term incentive compensation pursuant to our employment agreement with him. Under this arrangement, Mr. Pfeifle received a payment of \$400,000 at the end of fiscal 2003 and an additional payment of \$800,000 at the end of fiscal 2004, which constituted the maximum payout under the arrangement. Mr. Pfeifle is not entitled to receive any future payouts of long-term incentive compensation pursuant to our employment agreement with him. We refer you to "Employment Agreements and Other Compensation Arrangements—Employment Agreements" for information on this compensation arrangement and payout schedule.

Long Term Incentive Plan/Awards in Last Fiscal Year

Name	Number of Shares, Units or Other Rights(#)	Performance or Other Period Until Maturation or Payout	Estimated Future Payouts under Non-Stock-Price-Based Plans		
			Threshold (\$ or #)	Target (\$ or #)	Maximum (\$ or #)
Jeffrey Pfeifle	\$ 800,000	1/31/03–4/30/05	—	—	—

Employment and Other Agreements

Millard Drexler. Mr. Drexler has a services agreement with the Company pursuant to which he will serve as Chief Executive Officer for five years beginning on January 27, 2003, provided that Mr. Drexler can step down as Chief Executive Officer after January 2006 and serve only as Executive Chairman. The agreement provides for a minimum annual base salary of \$200,000, an annual bonus based on the achievement of earnings objectives to be determined each year, and reimbursement of business expenses, provided that such total compensation not exceed \$700,000 per year. The agreement also provides for (i) the grant of options to purchase 557,926 shares of Group common stock at an exercise price equal to \$6.82 per share, which we refer to as initial options, and (ii) the grant of premium options to purchase an additional 836,889 shares at an exercise price equal to \$25.00 per share and 836,889 shares at an exercise price equal to \$35.00 per share, which we refer to as premium options. The initial options and the premium options vest in equal annual installments over four years commencing on the second anniversary of the grant date. The agreement also provides for the grant of 55,793 immediately vested shares of Group common stock and the grant of 725,303 shares of Group common stock, which we refer to as the Drexler Restricted Shares. Mr. Drexler paid Group \$200,000 for the initial options and \$800,000 for the Drexler Restricted Shares. Under the agreement, Mr. Drexler is subject to customary non-solicitation, non-compete and confidentiality covenants.

Pursuant to the agreement, if Mr. Drexler's employment is terminated without "cause" or for "good reason" (each as defined in the services agreement), Mr. Drexler will be entitled to receive his base salary for one year, the immediate vesting of any unvested Drexler Restricted Shares and the immediate vesting of that portion of the initial options and the premium options that would have become vested and exercisable on the anniversary of the grant date immediately following the termination date. If such termination occurs after a "change in control" (as defined in the services agreement), all of the unvested initial options and premium options will immediately vest and become exercisable.

In September 2003, Mr. Drexler surrendered all of his premium options to the Company. In consideration of the surrender, we granted to Mr. Drexler replacement premium options in May 2004 as follows: options to purchase 836,889 shares at an exercise price equal to \$15.00 per share and options to purchase an additional 836,889 shares at an exercise price equal to \$25.00 per share. The replacement premium options have the same vesting schedule and other terms and conditions as the surrendered premium options. This option repricing was approved by a majority of the Board of Directors.

We refer you to footnote (c) to the Executive Compensation Table for information on the Drexler Restricted Shares and vesting thereof.

Roxane Al-Fayez. Ms. Al-Fayez has an offer letter, dated September 15, 2003, pursuant to which she will serve as Executive Vice-President of Direct Operations. The letter provides for an annual base salary of \$375,000, a one-time sign-bonus of \$50,000 payable after her start date and a one-time bonus of \$50,000 payable in October 2004, and an annual bonus based on the achievement of earnings objectives and individual performance goals to be determined each year, provided that the minimum bonus payable for fiscal year 2003 would be \$50,000. The agreement also provides for (i) the grant of options to purchase 50,000 shares of Group common stock, which we refer to as initial options, and (ii) the grant of 25,000 shares of Group common stock, which we refer to as the Al-Fayez Restricted Shares. The initial options have an exercise price of \$6.82 per share and vest in equal annual installments over four years commencing on the first anniversary of the grant date. Ms. Al-Fayez received relocation benefits and also receives a monthly housing allowance of \$3,000 and reimbursement for certain commuting expenses.

We refer you to footnote (i) to the Executive Compensation Table for information on the Al-Fayez Restricted Shares and vesting thereof.

Tracy Gardner. Ms. Gardner has an employment agreement with the Company pursuant to which she will serve as Executive Vice-President, Merchandising, Planning and Production for four years beginning in March 2004, subject to renewal upon mutual agreement. The agreement provides for a minimum annual base salary of \$450,000, a one-time sign-on bonus of \$100,000, and an annual bonus based on the achievement of earnings objectives and individual performance goals to be determined each year, provided that the minimum bonus payable for fiscal year 2004 would be \$112,500. The agreement also provides for (i) the grant of options to purchase 50,000 shares of Group common stock at an exercise price equal to \$6.82 per share, which we refer to as initial options, and (ii) the grant of premium options to purchase an additional 20,000 shares of Group common stock at an exercise price equal to \$15.00 per share and 20,000 shares of Group common stock at an exercise price equal to \$25.00 per share, which we refer to as premium options. The agreement also provides for the grant in March 2005 of (x) an additional option to purchase 20,000 shares of Group common stock at an exercise price equal to \$15.00 per share and (y) an additional option to purchase 20,000 shares of Group common stock at an exercise price equal to \$25.00 per share, which we refer to as the additional premium options. The initial options vest in equal annual installments over four years commencing on the first anniversary of the grant date. The premium options and the additional premium options vest in equal installments over four years commencing on the second anniversary of their respective grant dates. The agreement also provides for the grant of 50,000 shares of Group common stock, which we refer to as the Gardner Restricted Shares. Ms. Gardner also received relocation benefits in connection with her relocation to the New York area. Under the agreement, Ms. Gardner is subject to customary non-solicitation, non-compete and confidentiality covenants.

We refer you to footnote (k) to the Executive Compensation Table for information on the vesting of the Gardner Restricted Shares and vesting thereof.

Pursuant to the agreement, if Ms. Gardner's employment is terminated without "cause" or for "good reason" (each as defined in the employment agreement), Ms. Gardner will be entitled to receive her base salary for one year and a pro-rated amount of any bonus that she would have otherwise received for the fiscal year ending before the termination date. However, Ms. Gardner's right to the continuation of her base salary for one year will terminate upon the date that she becomes employed by a new employer or otherwise begins providing services for another entity, provided that if the cash compensation she receives pursuant thereto is less than her base salary in effect immediately prior to her termination date, she will be entitled to receive such incremental amount during the remainder of the severance period.

Jeffrey Pfeifle. Mr. Pfeifle has an employment agreement with the Company pursuant to which he will serve as President for five years beginning on February 1, 2003, subject to automatic one-year renewals. The agreement provides for a minimum annual base salary of \$760,000, one-time bonuses in the total amount of \$2,000,000 payable after his commencement date, an annual bonus based on the achievement of earnings objectives to be determined each year provided that the minimum bonus payable for fiscal year 2003 would be \$400,000, a long-term cash incentive payment between \$800,000 and \$1,200,000 based on the achievement of performance objectives to be determined each year payable in installments at the end of fiscal years 2003 and 2004, and reimbursement of business expenses. The agreement also provides for (i) the grant of options to purchase 167,378 shares of Group common stock at an exercise price equal to \$6.82 per share, which we refer to as initial options, and (ii) the grant of premium options to purchase an additional 111,585 shares at an exercise price equal to \$25.00 per share and 111,585 shares at an exercise price equal to \$35.00 per share, which we refer to as premium options. The initial options and the premium options vest in equal annual installments over four years commencing on the second anniversary of the grant date. The agreement also provides for the grant of 111,585 shares of Group common stock, which we refer to as the Pfeifle Restricted Shares.

Under the agreement, Mr. Pfeifle is subject to customary non-solicitation, non-compete and confidentiality covenants.

Pursuant to the agreement, if Mr. Pfeifle's employment is terminated without "cause" or for "good reason" (each as defined in the employment agreement), Mr. Pfeifle will be entitled to receive his base salary for two years, a pro-rated amount of any bonus that he would have otherwise received for the fiscal year ending before the termination date, and the immediate vesting of that portion of the initial options, premium options and Pfeifle Restricted Shares that would have become vested and exercisable on the anniversary of the grant date immediately following the termination date. If such termination occurs after a "change in control" (as defined in the services agreement) or within six months before a "change in control" if in contemplation thereof, all of the unvested initial options, premium options and Pfeifle Restricted Shares will immediately vest and become exercisable. If such termination occurs before February 1, 2006, Mr. Pfeifle is entitled to receive a minimum of \$2,000,000 in the form of cash severance compensation.

In September 2003, Mr. Pfeifle received surrendered all of his premium options to the Company. In consideration of the surrender, we granted to Mr. Pfeifle replacement premium options in May 2004 as follows: options to purchase 111,585 shares at an exercise price equal to \$15.00 per share and options to purchase an additional 111,585 shares at an exercise price equal to \$25.00 per share. The replacement premium options have the same vesting schedule and other terms and conditions as the surrendered premium options. This option repricing was approved by a majority of the Board of Directors.

We refer you to footnote (f) to the Executive Compensation Table for information on the Pfeifle Restricted Shares and the vesting thereof.

Company Bonus Plan

On April 12, 2005, the Compensation Committee of the Company's Board of Directors approved the financial goals under the J.Crew Group, Inc. bonus plan for fiscal 2005 (2005 Plan) for the annual cash bonus awards payable to our eligible employees participating in the 2005 Plan with respect to fiscal year 2005, including Messrs. Drexler, Hyatt and Pfeifle and Mss. Al-Fayez and Gardner. The fiscal 2005 bonuses payable under the 2005 Plan will be based on to the extent to which we meet or exceed specific financial goals established by the Compensation Committee and individual performance assessments as determined in the our discretion. For Messrs. Drexler, Hyatt and Pfeifle and Mss. Al-Fayez and Gardner, the amount of the actual bonus award could range from zero to 100% of his or her annual base salary, with targets ranging from 35% to 50% of his or her annual base salary.

Executive Severance Arrangements

Mr. Hyatt has an agreement with the Company which provides that, in the event of a termination without "cause" (as defined in the agreement), he will receive a continuation of his base salary and medical benefits for a period of one year after the termination date and the payment of any bonus that he would otherwise have received for the fiscal year ending before the termination date.

Shareholders Agreements

The Drexler Restricted Shares, the Pfeifle Restricted Shares, the Al-Fayez Restricted Shares, the Gardner Restricted Shares and any shares of Group common stock acquired by any of the named executive officers described above pursuant to the exercise of options are subject to a shareholders' agreement providing for certain transfer restrictions, registration rights and customary tag-along and drag-along rights.

In addition, Mr. Drexler's shareholders' agreement provides him with certain rights to appoint three directors by himself and three additional directors by mutual agreement with Texas Pacific Group, right to consent to our operating/capital budgets and certain anti-dilution and co-investment rights.

Compensation Committee Interlocks and Insider Participation

In fiscal 2004, the members of our Compensation Committee were Messrs. Coulter (Chairman) and Sloan and Ms. Woods. Ms. Woods is a former Chairman, former Chief Executive Officer and former Vice-Chairman of the Company.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth information regarding the beneficial ownership of the common stock of Group as of April 1, 2005 for each person who is known to the Company to be the beneficial owner of 5% or more of Group common stock. The holders listed have sole voting power and investment power over the shares held by them, except as indicated by the notes following the table.

Title of Class	Name and address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
Common stock	TPG Partners II, L.P. 301 Commerce Street, Suite 3300 Fort Worth, TX 76102	8,932,291 shares(a)(d)	51%
Common stock	Emily Woods J. Crew Group, Inc. 770 Broadway New York, NY 10003	2,767,377 shares(b)	16%
Common stock	Millard S. Drexler J. Crew Group, Inc. 770 Broadway New York, NY 10003	2,639,700 shares(c)	15%

- (a) These shares of common stock are beneficially owned by Texas Pacific Group and the following affiliates of Texas Pacific Group (collectively, TPG Affiliates): TPG Parallel II L.P., TPG Partners II L.P., TPG Investors II, L.P., and TPG Bacchus II, LLC.
- (b) Includes 497,200 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable.
- (c) Includes (i) 200,755 shares owned by Mr. Drexler; (ii) 262,524 restricted shares beneficially owned by a family trust of which Mr. Drexler is a trustee; (iii) 557,928 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable; and (iv) 1,618,494 shares not currently owned but which are issuable to Mr. Drexler's company upon his exercise of a right to exchange a loan made to the Company into shares of Group common stock at an exercise price equal to \$6.82 per share anytime prior to its maturity date in 2008. We refer you to "Certain Relationships and Related Transactions—TPG-MD Investment Notes Payable" for more information.
- (d) Includes 1,618,494 shares not currently owned but which are issuable to TPG Bacchus II, LLC upon its exercise of a right to exchange a loan made to the Company into shares of Group common stock at an exercise price equal to \$6.82 per share anytime prior to its maturity date in 2008. We refer you to "Certain Relationships and Related Transactions—TPG-MD Investment Notes Payable" for more information.

The following table sets forth information regarding the beneficial ownership of each class of equity securities of Group as of April 1, 2005 for (a) each director, (b) each of the named executive officers and (c) all directors and executive officers as a group.

The holders listed have sole voting power and investment power over the shares held by them, except as indicated by the notes following the table.

Title of Class	Name of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
Common stock	Richard Boyce	55,200(a)	*
Common stock	Jonathan Coslet	8,932,211(b)	51%
Common stock	James Coulter	8,932,211(b)	51%
Common stock	Steven Grand-Jean	12,500(c)	*
Common stock	Thomas Scott	12,500(c)	*
Common stock	Stuart Sloan	12,500(c)	*
Common stock	Josh Weston	32,978(d)	*
Common stock	Emily Woods	2,767,377(e)	16%
Common stock	Millard Drexler	2,639,700(f)	15%
Common stock	Roxane Al-Fayez	15,000(g)	*
Common stock	Tracy Gardner	0	*
Common stock	Scott Hyatt	31,000(a)	*
Common stock	Jeffrey Pfeifle	178,539(h)	1%
Common stock	All directors and executive officers as a group	14,689,505	84%
Series A preferred stock	Jonathan Coslet	73,475(b)	79%
Series A preferred stock	James Coulter	73,475(b)	79%
Series A preferred stock	Josh Weston	60	*
Series A preferred stock	Emily Woods	2,979	3%
Series A preferred stock	All directors and executive officers as a group	76,514	83%

* Represents less than 1% of the class.

(a) These are shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days.

(b) Attributes ownership of the shares beneficially owned by TPG Affiliates to Messrs. Coslet and Coulter, who are partners of Texas Pacific Group. Includes 1,618,494 shares not currently owned but which are issuable to TPG Bacchus II, LLC upon the exercise of a right to exchange a loan made to the Company into shares of Group common stock at an exercise price equal to \$6.82 per share anytime prior to its maturity date in 2008. We refer you to "Certain Relationships and

Related Transactions—TPG-MD Investment Notes Payable" for more information. Messrs. Coslet and Coulter disclaim beneficial ownership of the shares owned by TPG Affiliates.

- (c) Includes 7,500 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days.
- (d) Includes 2,500 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days.
- (e) Includes 497,200 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days.
- (f) Includes (i) 200,755 shares owned by Mr. Drexler; (ii) 262,524 shares beneficially owned by a family trust of which Mr. Drexler is a trustee; (iii) 557,928 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days; and (iv) 1,618,494 shares not currently owned but which are issuable to Mr. Drexler's company upon his exercise of a right to exchange a loan made to the Company into shares of Group common stock at an exercise price equal to \$6.82 per share anytime prior to its maturity date in 2008. We refer you to "Certain Relationships and Related Transactions—TPG-MD Investment Notes Payable" for more information.
- (g) Includes 8,750 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days.
- (h) Includes 97,639 shares not currently owned but which are issuable upon the exercise of stock options awarded under our stock option plan that are currently exercisable or become exercisable within 60 days.

We know of no arrangements, including any pledge by any person of our securities, the operation of which may at a subsequent date result in a change in control of the Company.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Tax Sharing Arrangement

Group and its subsidiaries entered into a tax sharing agreement providing (among other things) that each of the subsidiaries will reimburse Group for its share of income taxes determined as if such subsidiary had filed its tax returns on a "separate return" basis.

TPG-MD Investment Notes Payable

On February 4, 2003, Operating entered into a credit agreement with TPG-MD Investment, LLC, an entity controlled by Texas Pacific Group, our majority shareholder, and Millard Drexler, our Chief Executive Officer and Chairman of the Board, which provides for:

- Tranche A loan in an aggregate principal amount of \$10.0 million; and
- Tranche B loan in an aggregate principal amount of \$10.0 million.

The loans are due in February 2008 and bear interest at 5.0% per annum payable semi-annually in arrears on January 31 and July 31, commencing on July 31, 2003. Interest will compound and be capitalized and added to the principal amount on each interest payment date. The loans are guaranteed by certain subsidiaries of Operating.

The lender has the right, exercisable at anytime prior to the maturity date, to exchange the principal amount of and accrued and unpaid interest on the loans into shares of common stock of Group at an exercise price of \$6.82 per share. The lender also has the right to require Operating to prepay the Tranche B loan without premium or penalty under certain circumstances.

In November 2004, the credit agreement with TPG-MD Investment, LLC was amended to subordinate the Tranche A loan in right of payment to Operating's 9³/₄% Senior Subordinated Notes due 2014 while the Tranche B loan is *pari passu* in right of payment with such notes.

Under the terms of TPG-MD Investment, LLC's operating agreement, the distributions payable to Mr. Drexler under this credit agreement go directly to MDJC LLC, an entity whose sole members are Mr. Drexler and Grand-Jean Capital Management, which in turn is owned by Steven Grand-Jean, a Director of the Company. As payment for certain financial advisory services that Mr. Grand-Jean rendered to Mr. Drexler and pursuant to MDJC LLC's operating agreement, Mr. Grand-Jean is entitled to distributions under certain circumstances from his equity interest in MDJC LLC.

University Village Lease

Stuart Sloan, a Director, is the President of UV, Inc., which is the general partner of University Village Limited Partnership, the owner and operator of University Village Shopping Center in Seattle, Washington. On October 14, 2003, we entered into a lease agreement with University Village Limited Partnership with respect to the lease of 7,400 square feet at the University Village Shopping Center for the operation of one of our retail stores. The term of the lease is 10 years. We received an allowance for tenant's improvements in the amount of \$450,000 from University Village Limited Partnership. Annual rent due under the lease is comprised of (i) base rent payment of \$296,000 for years one through five and \$320,000 for years six through ten and (ii) contingent rent payment based on the store's sales in excess of a specified threshold. The lease also requires us to pay real estate taxes, insurance and certain common area costs. We believe that the lease contains terms reached pursuant to arms-length negotiations. Mr. Sloan's sons are the beneficiaries of trusts that are limited partners of University Village Limited Partnership.

Plum TV Sponsorship Agreement

Thomas Scott, a Director, is a founding partner, Chief Executive Officer and Executive Co-Chairman of Plum TV, LLC, a television station network operating in select resort markets. In May 2004, we entered into a sponsorship agreement with Plum TV pursuant to which Plum TV provided us with airtime on its network to televise commercials. The term of the agreement is one year and is scheduled to expire on May 31, 2005, although we currently plan to extend this arrangement. In fiscal 2004, we paid Plum TV, LLC a total amount of \$275,000, which we believe is the fair market value of the services provided. Emily Woods, also a Director, is married to Mr. Scott.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Audit Fees. The aggregate fees billed to us by the independent registered public accounting firm, KPMG LLP, for professional services rendered in connection with the audit of our financial statements included in this Annual Report on Form 10-K for fiscal 2004, and for review of our statements included in our Quarterly Reports on Form 10-Q during fiscal 2004, totaled approximately \$740,000. The aggregate fees billed to us by KPMG for professional services rendered in connection with the audit of our financial statements included in our Annual Report on Form 10-K for fiscal 2003, and for the review of our financial statements included in our Quarterly Reports on Form 10-Q during fiscal 2003, totaled approximately \$668,350.

Audit-Related Fees. The aggregate fees billed to us by KPMG for assurance and related services that are reasonably related to the performance of the audit and review of our financial statements that

are not already reported in the paragraph immediately above totaled approximately \$279,300 for fiscal 2003. These costs primarily related to services provided in connection with our exchange offer of outstanding 13¹/₈% Senior Discount Debentures for 16% Senior Discount Contingent Principal Notes, which was completed in May 2003. There were no audit-related fees in fiscal 2004.

Pre-Approval Policy. The Audit Committee has established policies on the pre-approval of audit and other services that the independent auditor may perform for the Company. The Committee must pre-approve the annual audit fees payable to the independent auditor on an annual basis. The Committee must also approve on a case-by-case basis their engagement for any other work to be performed for the Company that is not an integral component of the audit services as well as the compensation payable to the independent auditor therefore.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) 1. Financial Statements

The following financial statements are included in Item 8:

- (i) Report of KPMG LLP, Independent Registered Public Accounting Firm
J. Crew Group, Inc. and subsidiaries
- (ii) Consolidated Balance Sheets as of January 29, 2005 and January 31, 2004
- (iii) Consolidated Statements of Operations—Years ended January 29, 2005, January 31, 2004 and February 1, 2003
- (iv) Consolidated Statements of Changes in Stockholders' Deficit—Years ended January 29, 2005, January 31, 2004 and February 1, 2003
- (v) Consolidated Statements of Cash Flows—Years ended January 29, 2005, January 31, 2004 and February 1, 2003
J. Crew Operating and subsidiaries
- (vi) Consolidated Balance Sheets as of January 29, 2005 and January 31, 2004
- (vii) Consolidated Statements of Operations—Years ended January 29, 2005, January 31, 2004 and February 1, 2003
- (xii) Consolidated Statements of Changes in Stockholder's Deficit/Equity—Years ended January 29, 2005, January 31, 2004 and February 1, 2003
- (xiii) Consolidated Statements of Cash Flows—Years ended January 29, 2005, January 31, 2004 and February 1, 2003

Notes to consolidated financial statements

2. Financial Statement Schedules

Schedule II Valuation and Qualifying Accounts.

3. Exhibits

The exhibits listed on the accompanying Exhibit Index are incorporated by reference herein and filed as part of this report.

(b) Reports on Form 8-K

The Company filed the following reports on Form 8-K during the quarter ended January 29, 2005:

Current Report on Form 8-K was filed on November 23, 2004 relating to the Company's entry into a new Senior Subordinated Loan Agreement with entities managed by Black Canyon Capital LLC and Canyon Capital Advisors LLC (Black Canyon Loan Agreement) and the Company's announced redemption in full of its 10³/₈% senior subordinated notes and redemption in part of its 16% senior discount contingent principal notes (Redemption).

Current Report on Form 8-K was filed on December 1, 2004 relating to the Company's entry into a commitment letter with Wachovia Bank, N.A. and Congress Financial Corporation to refinance its existing working capital credit facility.

Current Report on Form 8-K was filed on December 9, 2004 relating to the Company's financial results for the period ended October 30, 2004.

Current Report on Form 8-K was filed on December 23, 2004 relating to the Company's announced redemption of its remaining 16% senior discount contingent principal notes (Second Redemption).

Current Report on Form 8-K was filed on December 28, 2004 relating to the Company's borrowing under the Black Canyon Loan Agreement, entry into related agreements, entry into the Amended Wachovia Credit Facility and the consummation of the Redemption.

Current Report on Form 8-K was filed on January 24, 2005 relating to the consummation of the Second Redemption.

(c) Exhibit Index

EXHIBIT INDEX

Articles of Incorporation and By-Laws

- 3.1 Restated Certificate of Incorporation of J. Crew Group, Inc. Incorporated by reference to Exhibit 3.1 to the Registration Statement on Form S-4, File No. 333-42427, filed December 16, 1997 (Group Registration Statement).
- 3.2 By-laws of J. Crew Group, Inc., as amended. Incorporated by reference to Exhibit 3.2 to the Form 10-K for the fiscal year ended February 3, 2001.
- 3.3 Certificate of Incorporation of J. Crew Operating Corp., as amended. Incorporated by reference to Exhibits 3.1 and 3.2 to the Registration Statement on Form S-4, File No. 333-4243, filed December 16, 1997 (Operating Registration Statement).
- 3.4 By-laws of J. Crew Operating Corp., as amended. Incorporated by reference to Exhibit 3 to the Form 10-Q for the period ended October 31, 1998 and Exhibit 3.14 to the Operating Registration Statement.

Instruments Defining the Rights of Security Holders, Including Indentures

- 4.1 Indenture, dated as of October 17, 1997, between J. Crew Group, Inc. and State Street Bank and Trust Company. Incorporated by reference to Exhibit 4.3 to the Group Registration Statement.
- 4.2 Indenture, dated as of October 17, 1997, between J. Crew Operating Corp. and State Street Bank and Trust Company. Incorporated by reference to Exhibit 4.1 to the Operating Registration Statement.
- 4.3 Registration Rights Agreement, dated as of October 17, 1997, by and among J. Crew Group, Inc., Donaldson, Lufkin & Jenrette Securities Corporation and Chase Securities Inc. Incorporated by reference to Exhibit 4.10 to the Group Registration Statement.
- 4.4 Stockholders' Agreement, dated as of October 17, 1997, between J. Crew Group, Inc. and the Stockholder signatories thereto. Incorporated by reference to Exhibit 4.1 to the Group Registration Statement.
- 4.5(a) Stockholders' Agreement, dated as of October 17, 1997, among J. Crew Group, Inc., TPG Partners II, L.P. and Emily Woods. Incorporated by reference to Exhibit 10.1 to the Group Registration Statement.
- 4.5(b) Amendment to Stockholders' Agreement, dated as of February 3, 2003, among J. Crew Group, Inc., TPG Partners II, L.P. and Emily Woods. Incorporated by reference to Exhibit 4.1 of the Form 8-K filed on February 7, 2003.
- 4.6 Stockholders' Agreement, dated as of September 9, 2002, between J. Crew Group, Inc., TPG Partners II, L.P. and Kenneth Pilot. Incorporated by reference to Exhibit 4.6 to the Form 10-K for fiscal year ended February 1, 2003.
- 4.7 Stockholders' Agreement, dated as of January 24, 2003, among J. Crew Group, Inc., TPG Partners II, L.P. and Millard Drexler. Incorporated by reference to Exhibit 4.1 of the Form 8-K filed on February 3, 2003.
- 4.8 Stockholders' Agreement, dated as of February 20, 2003, among J. Crew Group, Inc., TPG Partners II, L.P. and Jeffrey Pfeifle. Incorporated by reference to Exhibit 4.1 of the Form 8-K filed on February 26, 2003.

- 4.9 Stockholders' Agreement, dated as of February 12, 2003, among J. Crew Group, Inc., TPG Partners II, L.P. and Scott Gilbertson. Incorporated by reference to Exhibit 4.1 of the Form 8-K filed on February 14, 2003.

Material Contracts

- 10.1(a) Loan and Security Agreement, dated as of December 23, 2002, by and among J. Crew Operating Corp., J. Crew Inc., Grace Holmes, Inc. and H.F.D. No. 55, Inc. as Borrowers, J. Crew Group, Inc. and J. Crew International, Inc. as Guarantors, Wachovia Bank, National Association as Arranger, Congress Financial Corporation as Administrative and Collateral Agent, and the Lenders. Incorporated by reference to Exhibit 10.1 of the Form 8-K filed on December 27, 2002.
- 10.1(b) Amendment No. 1, dated as of February 7, 2003, to the Loan and Security Agreement. Incorporated by reference to Exhibit 10.1 of the Form 8-K filed on February 14, 2003.
- 10.1(c) Amendment No. 2, dated as of April 4, 2003, to the Loan and Security Agreement. Incorporated by reference to Exhibit 10.1 of the Form 8-K filed on April 8, 2003.
- 10.1(d) Amendment No. 3, dated as of November 21, 2004, to the Loan and Security Agreement. Incorporated by reference to Exhibit 4.5 of the Form 8-K filed on December 28, 2004.
- 10.1(e) Amended and Restated Loan and Security Agreement, dated as of December 23, 2004, by and among J.Crew Group, Inc., J. Crew Intermediate LLC, J. Crew Operating Corp. and certain subsidiaries thereof, Wachovia Capital Markets LLC as sole lead arranger and sole lead bookrunner, Wachovia Bank, National Association as Arranger, Congress Financial Corporation as Administrative Agent and Collateral Agent, and the Lenders. Incorporated by reference to Exhibit 4.6 of the Form 8-K filed on December 28, 2004.
- 10.2(a) Credit Agreement, dated as of February 4, 2003, by and between J.Crew Group, Inc., J.Crew Operating Corp., and certain subsidiaries thereof, and TPG-MD Investment, LLC. Incorporated by reference to Exhibit 10.1 of the Form 8-K filed on February 7, 2003.
- 10.2(b) Amendment No. 1, dated as of November 21, 2004, to the Credit Agreement. Incorporated by reference to Exhibit 4.4 of the Form 8-K filed on December 28, 2004.
- 10.3 Senior Subordinated Loan Agreement, dated as of November 21, 2004, among J. Crew Operating Corp. as Borrower, and certain subsidiaries of J. Crew Operating Corp. as Guarantors, the Lenders, and U.S. Bank National Association as Administrative Agent. Incorporated by reference to Exhibit 4.1 of the Form 8-K filed on December 28, 2004.
- 10.4 Security Agreement, dated as of November 21, 2004, among J. Crew Operating Corp., the grantors named therein and U.S. Bank National Association as Collateral Agent. Incorporated by reference to Exhibit 4.2 of the Form 8-K filed on December 28, 2004.
- 10.5 Intercreditor Agreement, dated as of November 21, 2004, among J. Crew Operating Corp., J.Crew Intermediate LLC and certain subsidiaries of J. Crew Operating Corp., Congress Financial Corporation as Senior Credit Agent, and U.S. Bank National Association as Collateral Agent.

Management Contracts and Compensatory Plans and Arrangements

- 10.6 Amended and Restated J. Crew Group, Inc. 1997 Stock Option Plan. Incorporated by reference to Exhibit 10.1 to the Form 10-Q for the period ended August 3, 2002.

- 10.7(a) J. Crew Group, Inc. 2003 Equity Incentive Plan (the "2003 Plan"). Incorporated by reference to Exhibit 10.4 to the Form 10-K for the fiscal year ended February 1, 2003.
- 10.7(b) Amendment No. 1 to the 2003 Plan. Incorporated by reference to Exhibit 10.4(b) to Form 10-K for the fiscal year ended January 31, 2004.
- 10.8 Separation Agreement, dated April 29, 2002, between the Company and Mark Sarvary. Incorporated by reference to Exhibit 10.5(d) to the Form 10-K for the fiscal year ended February 1, 2003.
- 10.9(a) Services Agreement, dated January 24, 2003, between the Company, Millard S. Drexler, Inc. and Millard Drexler. Incorporated by reference to Exhibit 10.9 to the Form 10-K for the fiscal year ended February 1, 2003.
- 10.9(b) Option Surrender Agreement, dated September 25, 2003, between the Company and Millard Drexler. Incorporated by reference to Exhibit 10.9(b) to the Form 10-K for the fiscal year ended January 31, 2004.
- 10.9(c) Stock Option Grant Agreement with respect to certain replacement options, dated as of May 12, 2004, between the Company and Millard Drexler. Incorporated by reference to Exhibit 10.1 to Form 10-Q for the quarter ended July 31, 2004.
- 10.10(a) Employment Agreement, dated January 24, 2003, between the Company and Jeffrey Pfeifle. Incorporated by reference to Exhibit 10.10 to the Form 10-K for the fiscal year ended February 1, 2003.
- 10.10(b) Option Surrender Agreement, dated September 25, 2003, between the Company and Jeffrey Pfeifle. Incorporated by reference to Exhibit 10.10(b) to the Form 10-K for the fiscal year ended January 31, 2004.
- 10.10(c) Stock Option Grant Agreement with respect to certain replacement options, dated as of May 12, 2004, between the Company and Jeffrey Pfeifle. Incorporated by reference to Exhibit 10.2 to Form 10-Q for the quarter ended July 31, 2004.
- 10.11 Separation Agreement, dated January 20, 2004, between the Company and Scott Gilbertson. Incorporated by reference to Exhibit 10.11(b) to Form 10-K for the fiscal year ended January 31, 2004.
- 10.12 Form of Executive Severance Agreement between the Company and certain executives thereof. Incorporated by reference to Exhibit 10.14 to Form 10-K for the fiscal year ended February 2, 2002.
- 10.13 Employment Agreement, dated January 23, 2004, between the Company and Tracy Gardner. Incorporated by reference to Exhibit 10.14 to Form 10-K for the fiscal year ended January 31, 2004.
- 10.14 Separation Agreement, dated December 23, 2003, and letter agreement dated, January 26, 2004, between the Company and Kathy Boyer. Incorporated by reference to Exhibit 10.15 to Form 10-K for the fiscal year ended January 31, 2004.
- 10.15 Employment Agreement, dated April 10, 2004, between the Company and Amanda Bokman. Incorporated by reference to Exhibit 10.16 to Form 10-K for the fiscal year ended January 31, 2004.
- 10.16* Offer letter, dated September 15, 2003, from the Company to Roxane Al-Fayez.
- 10.17* Separation Agreement, dated October 22, 2004, between the Company and Paul Fusco.

- 10.18* Lease Agreement, dated October 14, 2004, between a subsidiary of J. Crew Group, Inc. and University Village Limited Partnership relating to the Company's store in the University Village Shopping Center in Seattle, WA, and Guaranty of J. Crew Group, Inc.

Other Exhibits

- 14 Code of Ethics and Business Practices of the Company. Incorporated by reference to Exhibit 14 to Form 10-K for the fiscal year ended January 31, 2004.
- 21.1 Subsidiaries of J. Crew Group, Inc. Incorporated by reference to Exhibit 21.1 to Form 10-K for the fiscal year ended January 31, 2004.
- 23.1* Consent of KPMG LLP, Independent Registered Public Accounting Firm.
- 31.1* Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2* Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1* Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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* Filed herewith

SIGNATURES

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

Date: April 29, 2005

J. CREW GROUP, INC.
J. CREW OPERATING CORP.

By: /s/ MILLARD S. DREXLER

Millard S. Drexler
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of each registrant and in the capacities indicated, on April 29, 2005.

Signature	Title
/s/ MILLARD DREXLER	Chairman of the Board, Chief Executive Officer and a Director (Principal Executive Officer)
Millard Drexler	
/s/ AMANDA BOKMAN	Executive Vice President and Chief Financial Officer (Principal Financial Officer)
Amanda Bokman	
/s/ NICHOLAS LAMBERTI	Vice President and Corporate Controller (Principal Accounting Officer)
Nicholas Lamberti	
/s/ RICHARD BOYCE	Director
Richard Boyce	
/s/ JONATHAN COSLET	Director
Jonathan Coslet	
/s/ JAMES COULTER	Director
James Coulter	
/s/ STEVEN GRAND-JEAN	Director
Steven Grand-Jean	

/s/ THOMAS SCOTT

Thomas Scott

Director

/s/ STUART SLOAN

Stuart Sloan

Director

/s/ JOSH WESTON

Josh Weston

Director

/s/ EMILY WOODS

Emily Woods

Director

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

J. Crew Group Inc, and J. Crew Operating Corp.

We have audited the consolidated financial statements of J. Crew Group Inc. ("Group") and J. Crew Operating Corp., a wholly owned subsidiary of Group ("Operating") (together referred to as the "Companies") as listed in the accompanying index. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Companies management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Companies are not required to have, nor were we engaged to perform, an audit of their internal controls over financial reporting. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Group and Operating as of January 29, 2005, and January 31, 2004 and the results of their operations and their cash flows for each of the years in the three-year period ended January 29, 2005, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Note 6 to the consolidated financial statements, in the third quarter of fiscal 2003, Group adopted Statement of Financial Accounting Standard No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity".

As discussed in Note 2, the Companies restated the consolidated statements of cash flows for the years ended January 31, 2004 and February 1, 2003, to reclassify the proceeds from construction allowances from cash flows from investing activities to cash flows from operating activities.

KPMG LLP
New York, New York
April 4, 2005

**J.CREW GROUP, INC. AND
SUBSIDIARIES**

Consolidated Balance Sheets

	January 29, 2005	January 31, 2004
	<u>(in thousands)</u>	<u>(in thousands)</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 23,647	\$ 49,650
Merchandise inventories	88,093	66,028
Prepaid expenses and other current assets	22,217	20,733
Refundable income taxes	9,320	9,320
	<u>143,277</u>	<u>145,731</u>
Total current assets	143,277	145,731
	<u>259,098</u>	<u>284,945</u>
Property and equipment—at cost	259,098	284,945
Less accumulated depreciation and amortization	(138,285)	(146,565)
	<u>120,813</u>	<u>138,380</u>
Other assets	14,104	13,500
	<u>278,194</u>	<u>297,611</u>
Total assets	\$ 278,194	\$ 297,611
Liabilities and Stockholders' Deficit		
Current liabilities:		
Current portion of long-term debt	\$ —	\$ 1,164
Accounts payable	68,569	49,386
Other current liabilities	61,148	47,789
Federal and state income taxes	1,392	1,175
	<u>131,109</u>	<u>99,514</u>
Total current liabilities	131,109	99,514
	<u>59,064</u>	<u>56,723</u>
Deferred credits	59,064	56,723
Long-term debt	576,933	516,640
	<u>92,800</u>	<u>92,800</u>
Preferred stock	92,800	92,800
Stockholders' deficit	(581,712)	(468,066)
	<u>278,194</u>	<u>297,611</u>
Total liabilities and stockholders' deficit	\$ 278,194	\$ 297,611

See accompanying notes to consolidated financial statements.

**J.CREW GROUP, INC. AND
SUBSIDIARIES**

Consolidated Statements of Operations

	Years Ended		
	January 29, 2005	January 31, 2004	February 1, 2003
	(in thousands)		
Revenues:			
Net sales	\$ 778,295	\$ 660,628	\$ 732,279
Other	25,921	29,337	36,065
	804,216	689,965	768,344
Cost of goods sold, including buying and occupancy costs	478,829	440,276	472,262
Gross profit	325,387	249,689	296,082
Selling, general and administrative expenses	287,745	280,464	301,718
Income/(loss) from operations	37,642	(30,775)	(5,636)
Interest expense—net	87,571	63,844	40,954
Insurance proceeds	—	(3,850)	(1,800)
(Gain)/loss on refinancing of debt (net of expenses of \$2,922 in 2003)	49,780	(41,085)	—
Loss before income taxes	(99,709)	(49,684)	(44,790)
Income taxes (provision)/benefit	(600)	(500)	4,200
Net loss	\$ (100,309)	\$ (50,184)	\$ (40,590)

See accompanying notes to consolidated financial statements.

**J.CREW GROUP, INC. AND
SUBSIDIARIES**

Consolidated Statements of Changes in Stockholders' Deficit

(in thousands, except shares)

	Common Stock		Additional paid-in capital	Accumulated deficit	Treasury stock	Deferred compensation	Stockholders' deficit
	Shares	Amount					
Balance at February 2, 2002	12,238,189	\$ 122	\$ 70,690	\$ (387,186)	\$ (2,351)	\$ (318)	\$ (319,043)
Net loss	—	—	—	(40,590)	—	—	(40,590)
Preferred stock dividends	—	—	—	(33,578)	—	—	(33,578)
Issuance of common stock	12,318	1	283	—	—	—	284
Issuance of restricted stock	1,109,266	11	1,100	—	—	(311)	800
Amortization of restricted stock	—	—	—	—	—	464	464
Balance at February 1, 2003	13,359,773	134	72,073	(461,354)	(2,351)	(165)	(391,663)
Net loss	—	—	—	(50,184)	—	—	(50,184)
Preferred stock dividends	—	—	—	(26,260)	—	—	(26,260)
Issuance of restricted stock	224,402	2	163	—	—	(165)	—
Amortization of restricted stock	—	—	—	—	—	41	41
Forfeiture of restricted stock	—	—	—	—	(62)	62	—
Balance at January 31, 2004	13,584,175	136	72,236	(537,798)	(2,413)	(227)	(468,066)
Net loss	—	—	—	(100,309)	—	—	(100,309)
Preferred stock dividends	—	—	—	(13,456)	—	—	(13,456)
Issuance of restricted stock	196,000	1	144	—	—	(145)	—
Amortization of restricted stock	—	—	—	—	—	119	119
Balance at January 29, 2005	13,780,175	\$ 137	\$ 72,380	\$ (651,563)	\$ (2,413)	\$ (253)	\$ (581,712)

See accompanying notes to consolidated financial statements.

**J.CREW GROUP, INC. AND
SUBSIDIARIES**

Consolidated Statements of Cash Flows

	Years Ended		
	January 29, 2005	January 31, 2004	February 1, 2003
		(restated)	(restated)
(in thousands)			
Cash flows from operating activities:			
Net loss	\$ (100,309)	\$ (50,184)	\$ (40,590)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation and amortization	37,061	43,075	43,197
Amortization of deferred financing costs	2,425	2,179	4,435
Non-cash interest expense (including redeemable preferred stock dividends of \$33,106 in 2004 and \$14,206 in 2003)	63,536	40,991	12,313
Deferred income taxes	—	5,000	7,421
Non-cash compensation expense	119	41	(589)
(Gain)/loss on refinancing of debt	49,780	(41,085)	—
Changes in operating assets and liabilities:			
Merchandise inventories	(22,065)	41,290	31,600
Prepaid expenses and other current assets	(1,484)	4,153	2,140
Other assets	664	832	(2,470)
Accounts payable and other liabilities	28,819	(23,211)	(13,531)
Federal and state income taxes	217	(4,845)	(12,140)
Net cash provided by operating activities	58,763	18,236	31,786
Cash flow from investing activities:			
Capital expenditures	(13,431)	(9,908)	(26,920)
Cash flow from financing activities:			
Proceeds from long-term debt	275,000	25,820	—
Costs incurred in refinancing debt	(22,137)	(2,617)	(3,256)
Repayment of long-term debt	(324,198)	(776)	—
Proceeds from the issuance of common stock	—	—	1,084
Net cash provided by (used in) financing activities	(71,335)	22,427	(2,172)
Increase (decrease) in cash and cash equivalents	(26,003)	30,755	2,694
Cash and cash equivalents at beginning of year	49,650	18,895	16,201
Cash and cash equivalents at end of year	\$ 23,647	\$ 49,650	\$ 18,895
Supplementary cash flow information:			
Income taxes paid	\$ 411	\$ 345	\$ 453
Interest paid	\$ 23,270	\$ 20,400	\$ 19,380
Non-cash financing activities:			
Dividends on preferred stock (charged directly to stockholder's deficit)	\$ 13,456	\$ 26,260	\$ 33,578
Interest payable on 13 ¹ / ₈ % Senior Discount Debentures at February 1, 2003 capitalized and added to the principal amount of the debt	—	\$ 4,416	—
Exchange of 16% Senior Discount Contingent Principal Notes of J.Crew Intermediate LLC with a fair value of \$87,006 for \$131,083 carrying value of 13 ¹ / ₈ % Senior Discount Debentures of J.Crew Group, Inc.	—	—	—

See accompanying notes to consolidated financial statements.

**J.CREW OPERATING CORP. AND
SUBSIDIARIES**

Consolidated Balance Sheets

	January 29, 2005	January 31, 2004
	(in thousands)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 23,647	\$ 49,650
Merchandise inventories	88,093	66,028
Prepaid expenses and other current assets	22,217	20,733
Refundable income taxes	9,320	9,320
Total current assets	143,277	145,731
Property and equipment—at cost	259,098	284,945
Less accumulated depreciation and amortization	(138,285)	(146,565)
	120,813	138,380
Due from J.Crew Group, Inc.	178,757	—
Other assets	13,971	11,091
Total assets	\$ 456,818	\$ 295,202
Liabilities and Stockholder's Deficit		
Current liabilities:		
Current portion of long-term debt	\$ —	\$ 1,164
Accounts payable	68,569	49,386
Other current liabilities	60,314	46,942
Federal and state income taxes	1,392	1,175
Total current Liabilities	130,275	98,667
Deferred credits	59,064	56,723
Long-term debt	297,000	174,880
Due to J.Crew Group, Inc.	—	5,897
Stockholder's deficit	(29,521)	(40,965)
Total liabilities and stockholder's deficit	\$ 456,818	\$ 295,202

See accompanying notes to consolidated financial statements.

**J.CREW OPERATING CORP. AND
SUBSIDIARIES**

Consolidated Statements of Operations

	Years Ended		
	January 29, 2005	January 31, 2004	February 1, 2003
	(in thousands)		
Revenues:			
Net sales	\$ 778,295	\$ 660,628	\$ 732,279
Other	25,921	29,337	36,065
	804,216	689,965	768,344
Costs of goods sold, including buying and occupancy costs	478,829	440,276	472,262
Gross profit	325,387	249,689	296,082
Selling, general and administrative expenses	287,704	280,423	301,254
Income/(loss) from operations	37,683	(30,734)	(5,172)
Interest expense—net	21,615	20,496	23,200
Loss on refinancing of debt	4,024	—	—
Insurance proceeds	—	(3,850)	(1,800)
Income/(loss) before income taxes	12,044	(47,380)	(26,572)
Income taxes—(provision)/benefit	(600)	5,410	17,750
Net income/(loss)	\$ 11,444	\$ (41,970)	\$ (8,822)

See accompanying notes to consolidated financial statements.

**J.CREW OPERATING CORP. AND
SUBSIDIARIES**

Statement of Changes in Stockholder's Equity/(Deficit)

	(in thousands)
Balance at February 2, 2002	\$ 19,147
Net loss	(8,822)
Balance at February 1, 2003	10,325
Net loss	(41,970)
Dividends to affiliates	(9,320)
Balance at January 31, 2004	(40,965)
Net income	11,444
Balance at January 29, 2005	\$ (29,521)

Note: Operating Corp. has authorized 100 shares of common stock, par value \$.01 per share, all of which were issued and outstanding during the three year period ended January 29, 2005.

See accompanying notes to consolidated financial statements.

**J.CREW OPERATING CORP. AND
SUBSIDIARIES**

Consolidated Statements of Cash Flows

	Years Ended		
	January 29, 2005	January 31, 2004	February 1, 2003
		(restated)	(restated)
	(in thousands)		
Cash flows from operating activities:			
Net income (loss)	\$ 11,444	\$ (41,970)	\$ (8,822)
Adjustments to reconcile net income/(loss) to net cash provided in operating activities:			
Depreciation and amortization	37,061	43,075	43,197
Amortization of deferred financing costs	1,855	1,724	4,202
Deferred income taxes	—	(910)	(4,694)
Non-cash compensation expense	—	—	(1,053)
Non-cash interest expense	1,000	1,000	—
Loss on refinancing of debt	4,024	—	—
Changes in operating assets and liabilities:			
Merchandise inventories	(22,065)	41,290	31,600
Prepaid expenses and other current assets	(1,484)	4,153	2,140
Other assets	664	832	(2,470)
Accounts payable and other liabilities	28,860	(23,267)	(18,719)
Federal and state income taxes	217	(4,845)	(13,409)
Net cash provided by operating activities	61,576	21,082	31,972
Cash flow from investing activities:			
Capital expenditures	(13,431)	(9,908)	(26,920)
Cash flow from financing activities:			
Proceeds from long-term debt	275,000	25,820	—
Transfers to affiliate	(184,654)	(5,463)	898
Costs incurred in refinancing debt	(9,450)	—	(3,256)
Repayment of long-term debt	(155,044)	(776)	—
Net cash provided by/(used in) financing activities	(74,148)	19,581	(2,358)
Increase/(decrease) in cash and cash equivalents	(26,003)	30,755	2,694
Cash and cash equivalents at beginning of year	49,650	18,895	16,201
Cash and cash equivalents at end of year	\$ 23,647	\$ 49,650	\$ 18,895

See accompanying notes to consolidated financial statements.

J.CREW GROUP, INC. AND SUBSIDIARIES

J.CREW OPERATING CORP. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Year Ended January 29, 2005
Dollars in thousands, unless otherwise indicated

1. Nature Of Business And Summary Of Significant Accounting Policies

(a) Basis of Presentation

The consolidated financial statements included herein are:

- (1) J.Crew Operating Corp. and its wholly-owned subsidiaries (Operating), which consist of the accounts of J.Crew Operating Corp and its wholly owned subsidiaries.
- (2) J.Crew Group, Inc. and its wholly owned subsidiaries (the Company or Group), which consist of the accounts of J.Crew Group, Inc. and its wholly-owned subsidiaries, including J.Crew Intermediate LLC (Intermediate) and Operating. Intermediate was formed in March 2003 as a limited liability company. Effective May 2003 Group transferred its investment in Operating to Intermediate.

All significant intercompany balances and transactions are eliminated in consolidation.

Except where otherwise specified all notes to the consolidated financial statements apply to both Operating and Group.

(b) Business

The Company designs, contracts for the manufacture of, markets and distributes men's and women's apparel, shoes and accessories under the J.Crew brand name. The Company's products are marketed, primarily in the United States, through various channels of distribution, including retail and factory outlet stores, catalogs, and the Internet. The Company is also party to a licensing agreement which grants the licensee exclusive rights to use the Company's trademarks in connection with the manufacture and sale of products in Japan. The license agreement provides for payments based on a specified percentage of net sales.

The Company is subject to seasonal fluctuations in its merchandise sales and results of operations. The Company expects its sales and operating results generally to be lower in the first and second quarters than in the third and fourth quarters (which include the back-to-school and holiday seasons) of each fiscal year.

A significant amount of the Company's products are produced in Asia through arrangements with independent contractors. As a result, the Company's operations could be adversely affected by political instability resulting in the disruption of trade from the countries in which these contractors are located or by the imposition of additional duties or regulations relating to imports or by the contractor's inability to meet the Company's production requirements.

(c) Segment Information

The Company operates in one reportable business segment. All of the Company's identifiable assets are located in the United States. Export sales are not significant.

(d) Fiscal Year

The Company's fiscal year ends on the Saturday closest to January 31. The fiscal years 2004, 2003 and 2002 ended on January 29, 2005, January 31, 2004 and February 1, 2003 and each fiscal year consisted of 52 weeks.

(e) Cash Equivalents

For purposes of the consolidated statements of cash flows, the Company considers all highly liquid debt instruments, with maturities of 90 days or less when purchased, to be cash equivalents. Cash equivalents, which were \$14,192 and \$43,312 at January 29, 2005 and January 31, 2004, respectively, are stated at cost, which approximates market value.

(f) Merchandise Inventories

Merchandise inventories are stated at the lower of average cost or market. The Company capitalizes certain design, purchasing and warehousing costs in inventory and these costs are included in cost of goods sold as the inventories are sold.

(g) Advertising and Catalog Costs

Direct response advertising, which consists primarily of catalog production and mailing costs, are capitalized and amortized over the expected future revenue stream. The Company accounts for catalog costs in accordance with the AICPA Statement of Position ("SOP") 93-7, "Reporting on Advertising Costs." SOP 93-7 requires that the amortization of capitalized advertising costs be the amount computed using the ratio that current period revenues for the catalog cost pool bear to the total of current and estimated future period revenues for that catalog cost pool. The capitalized costs of direct response advertising are amortized, commencing with the date catalogs are mailed, over the duration of the expected revenue stream, which was four months for the fiscal years 2002, 2003 and 2004. Deferred catalog costs, included in prepaid expenses and other current assets, as of January 29, 2005 and January 31, 2004 were \$6,478 and \$6,411, respectively. Catalog costs, which are reflected in selling and administrative expenses, for the fiscal years 2004, 2003 and 2002 were \$41,258, \$43,978 and \$56,695, respectively.

All other advertising costs, which are not significant, are expensed as incurred.

(h) Property and Equipment

Property and equipment are stated at cost and are depreciated over the estimated useful lives by the straight-line method. Buildings and improvements are depreciated over estimated useful lives of twenty years. Furniture, fixtures and equipment are depreciated over estimated useful lives, ranging from three to ten years. Leasehold improvements (including rent capitalized during the construction period) are amortized over the shorter of their useful lives or related lease terms (without consideration of optional renewal periods).

Systems development costs are capitalized and amortized on a straight-line basis over periods ranging from three to five years.

(i) *Debt Issuance Costs*

Debt issuance costs (included in other assets) are amortized over the term of the related debt agreements. Unamortized debt issuance costs are as follows:

	January 29, 2005	January 31, 2004
Group	\$ 132	\$ 2,409
Operating	7,897	3,966
Total	\$ 8,029	\$ 6,375

(j) *Income Taxes*

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes". This statement requires the use of the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred taxes are determined based on the difference between the financial reporting and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. The provision for income taxes includes taxes currently payable and deferred taxes resulting from the tax effects of temporary differences between the financial statement and tax bases of assets and liabilities.

(k) *Revenue Recognition*

Revenue is recognized for catalog and internet sales when merchandise is shipped to customers and at the time of sale for retail sales. Shipping terms for catalog and internet sales are FOB shipping point, and title passes to the customer at the time and place of shipment. Prices for all merchandise are listed in the Company's catalogs and website and are confirmed with the customer upon order. The customer has no cancellation privileges other than customary rights of return that are accounted for in accordance with SFAS No. 48 "*Revenue Recognition When Right of Return Exists*." The Company accrues a sales return allowance for estimated returns of merchandise subsequent to the balance sheet date that relate to sales prior to the balance sheet date. Amounts billed to customers for shipping and handling fees related to catalog and internet sales are included in other revenues at the time of shipment. Royalty revenue is recognized as it is earned based on contractually specified percentages applied to reported sales. Advance royalty payments are deferred and recorded as revenue when the related sales occur. Other revenues include estimated amount of unredeemed gift card liability based on Company specific historical trends, which amounted to \$1,410, \$1,676 and \$1,962 in fiscal years 2004, 2003, and 2002, respectively.

(l) *Operating Expenses*

Cost of goods sold (including buying and occupancy costs) includes the direct cost of purchased merchandise, inbound freight, design, buying and production costs, occupancy costs related to store operations and all shipping and handling and delivery costs associated with our J.Crew Direct business.

Selling, general and administrative expenses include all operating expenses not included in cost of goods sold, primarily catalog production and mailing costs, certain warehousing expenses, which aggregated \$10,816, \$9,860 and \$10,440 for fiscal years 2004, 2003 and 2002, respectively, administrative payroll, store expenses other than occupancy costs, depreciation and amortization and credit card fees.

(m) Store Pre-opening Costs

Costs associated with the opening of new retail and factory outlet stores are expensed as incurred.

(n) Derivative Financial Instruments

Derivative financial instruments have been used by the Company from time to time to manage its interest rate and foreign currency exposures. The Company does not enter into derivative financial instruments for speculative purposes. For interest rate swap agreements, the net interest paid is recorded as interest expense on a current basis. Gains or losses resulting from market fluctuations are not recognized. The Company from time to time enters into forward foreign exchange contracts as hedges relating to identifiable currency positions to reduce the risk from exchange rate fluctuations.

(o) Use of Estimates in the Preparation of Financial Statements

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

(p) Impairment of Long-Lived Assets

The Company reviews long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company assesses the recoverability of such assets based upon estimated cash flow forecasts. Charges of \$146, \$675 and \$137 were incurred in fiscal 2004, 2003 and 2002 to write-down the carrying value of certain long-lived assets.

(q) Stock Based Compensation

The Company accounts for stock-based compensation using the intrinsic value method of accounting for employee stock options as permitted by SFAS No. 123, "Accounting for Stock-Based Compensation". Accordingly, compensation expense is not recorded for options granted if the option price is equal to or in excess of the fair market price at the date of grant. If the Company had adopted the fair value recognition provisions of SFAS No. 123, the effect on net income would not be material.

Restricted stock awards result in the recognition of deferred compensation, which is charged to expense over the vesting period of the awards. Deferred compensation is presented as a reduction of stockholders' equity. Total compensation expense recorded with respect to stock-based compensation, all of which related to restricted stock awards, amounted to \$119, \$41 and \$464 in 2004, 2003 and 2002, respectively.

(r) *Deferred rent and lease incentives*

Rental payments under operating leases are charged to expense on a straight-line basis after consideration of step rent provisions and escalation clauses. Differences between rental expense and actual rental payments are recorded as deferred rent and included in deferred credits. The Company capitalizes rent expense during the period from possession date through the completion of store construction. Rent is expensed subsequent to the end of construction. Capitalized rent is amortized over the lease term (without consideration of optional renewal periods).

The Company receives construction allowances upon entering into certain store leases. These construction allowances are recorded as deferred credits and are amortized as a reduction of rent expense over the term of the related lease. Deferred construction allowances were \$39,250 and \$43,668 at January 29, 2005 and January 31, 2004, respectively.

(s) *Reclassification*

Certain prior year amounts have been reclassified to conform with current year's presentation.

2. Restatement

During the fourth quarter of fiscal 2004, the Company determined that it had misclassified proceeds from construction allowances in the consolidated statement of cash flows. As a result, the consolidated statements of cash flows for Group and Operating for the years ended January 31, 2004 and February 1, 2003 have been restated to reclassify the proceeds from construction allowances from cash flows from investing activities to cash flows from operating activities. There was no effect on the Company's consolidated balance sheet or consolidated statement of operations.

The effects of the reclassification are as follows:

	Year Ended	
	January 31, 2004	February 1, 2003
Accounts payable and other liabilities:		
Group:		
As reported	\$ (25,233)	\$ (20,033)
As restated	\$ (23,211)	\$ (13,531)
Operating:		
As reported	\$ (25,289)	\$ (25,221)
As restated	\$ (23,267)	\$ (18,719)
Cash flows from operating activities:		
Group:		
As reported	\$ 16,214	\$ 25,284
As restated	\$ 18,236	\$ 31,786
Operating:		
As reported	\$ 19,060	\$ 25,470
As restated	21,082	31,972
Proceeds from construction allowances:		
Group and Operating		
As reported	\$ 2,022	\$ 6,502
As restated	\$ —	\$ —
Cash flows from investing activities:		
Group:		
As reported	\$ (7,886)	\$ (20,418)
As restated	\$ (9,908)	\$ (26,920)
Operating:		
As reported	\$ (7,886)	\$ (20,418)
As restated	\$ (9,908)	\$ (26,920)

3. Insurance Proceeds

The terrorist events of September 11, 2001 resulted in the destruction of the Company's retail store located at the World Trade Center in New York City, resulting in the loss of inventories and store fixtures, equipment and leasehold improvements. These losses and the resulting business interruption were covered by insurance policies maintained by the Company.

The statement of operations for the years ended January 31, 2004 and February 1, 2003 include gains of \$3,850 and \$1,800 as a result of additional insurance recoveries. No additional insurance recoveries are payable to the Company relating to this loss.

4. Property and Equipment

Property and equipment, net consists of:

	January 29, 2005	January 31, 2004
Land	\$ 1,710	\$ 1,710
Buildings and improvements	11,712	11,705
Fixtures and equipment	68,811	90,898
Leasehold improvements	173,725	176,740
Construction in progress	3,140	3,892
	259,098	284,945
Less accumulated depreciation and amortization	138,285	146,565
	\$ 120,813	\$ 138,380

5. Other Current Liabilities

Other current liabilities consist of:

	January 29, 2005	January 31, 2004
Customer liabilities	\$ 14,095	\$ 9,089
Accrued catalog and marketing costs	801	2,505
Taxes, other than income taxes	3,115	3,046
Accrued interest(a)	3,664	5,330
Accrued occupancy	1,141	817
Reserve for sales returns	4,831	2,988
Accrued compensation	8,465	3,535
Other	25,036	20,479
	\$ 61,148	\$ 47,789

(a) includes \$2,830 and \$4,483 related to Operating

6. Lines of Credit

On December 23, 2004, Operating entered into an Amended and Restated Loan and Security Agreement with Wachovia Capital Markets LLC, as arranger, Wachovia Bank, National Association, as administrative agent, Bank of America NA, as syndication agent, and Congress Financial Corporation, as collateral agent, and a syndicate of lenders (the "Amended Wachovia Credit Facility") which provides for a maximum credit availability of up to \$170.0 million (which may be increased to \$250.0 million subject to certain conditions).

The Amended Wachovia Credit Facility provides for revolving loans and letter of credit accommodations. The Amended Wachovia Credit Facility expires in December 2009. The total amount of availability is subject to limitations based on specified percentages of eligible receivables, inventories and real property. As of January 29, 2005 excess availability under the Amended Wachovia Credit Facility was \$27.0 million.

Borrowings are secured by a perfected first priority security interest in all the assets of Intermediate and its subsidiaries and bear interest, at the Company's option, at the prime rate plus a margin of up to 0.25% or the Eurodollar rate plus a margin ranging from 1.25% to 2.00%. The Company is required to pay a monthly unused line fee ranging from .25% to .375%. Fees for outstanding commercial letters of credit range from .625% to 1.0% and fees for outstanding standby letters of credit are 1.25%.

The Amended Wachovia Credit Facility includes restrictions, including the incurrence of additional indebtedness, the payment of dividends and other distributions, the making of investments, the granting of loans and the making of capital expenditures. The Amended Wachovia Credit Facility permits restricted payments (by way of dividends or other distributions) with respect to, among other things, the Company's capital stock payable solely in additional shares of its capital stock, the Company's tax sharing agreement, the Series A Preferred Stock of Group, the Series B Preferred Stock of Group and the 13^{1/8}% Senior Discount Debentures due 2008 of Group. The ability of Operating to declare dividends on its capital stock is also limited by Delaware law, which permits a company to pay dividends on its capital stock only out of its surplus or, in the event that it has no surplus, out of its net profits for the year in which a dividend is declared or for the immediately preceding fiscal year. Under the Amended Wachovia Credit Facility, Operating is required to maintain a fixed interest charge coverage ratio of 1.1 if excess availability is less than \$20.0 million for any 30 consecutive day period. Operating has at all times been in compliance with all financial covenants.

Maximum borrowings under our working capital credit agreements were none, \$10,000 and \$63,000 and average borrowings were none, \$1,020 and \$40,400 during fiscal years 2004, 2003 and 2002, respectively. There were no borrowings outstanding at January 29, 2005 and January 31, 2004.

Outstanding letters of credit established primarily to facilitate international merchandise purchases at January 29, 2005 and January 31, 2004 amounted to \$58,700 and \$39,500.

7. Long-Term Debt and Preferred Stock

	January 29, 2005	January 31, 2004
Operating:		
9 ³ / ₄ % senior subordinated notes(a)	\$ 275,000	\$ —
5% notes payable(b)	22,000	21,000
10 ³ / ₈ % senior subordinated notes(c)	—	150,000
Wachovia credit facility	—	5,044
Less amount due within one year	—	(1,164)
Total Operating long-term debt	297,000	174,880
Intermediate:		
16% senior discount contingent principal notes (net of unamortized debt issuance discount of \$38,677)(d)	—	108,389
Group:		
13 ¹ / ₈ % senior discount debentures(e)	21,667	21,667
Mandatorily redeemable preferred stock(f)	258,266	211,704
Total Group long-term debt	576,933	516,640
Group preferred stock(f)	92,800	92,800
Total Group long-term debt and preferred stock	\$ 669,733	\$ 609,440

The scheduled payments of long term debt are \$43.7 million in 2008, \$258.3 million in 2009 and \$275.0 million in 2014.

(a) On November 21, 2004, Operating entered into a Senior Subordinated Loan Agreement with entities managed by Black Canyon Capital LLC and Canyon Capital Advisors LLC, which provided for a term loan of \$275 million. The proceeds of the term loan were used to redeem in full Operating's outstanding 10³/₈% senior subordinated notes due 2007 (\$150 million) and to redeem in part Intermediate's 16% senior discount contingent principal notes due 2008 (\$125 million). On March 18, 2005, the term loan was converted into equivalent new 9³/₄% senior subordinated notes of Operating due 2014 (9³/₄% senior subordinated notes) in accordance with the terms of the loan agreement.

The 9³/₄% senior subordinated notes are general senior subordinated obligations of the Operating and certain subsidiaries of Operating and Intermediate, are subordinated in right of payment to their existing and future senior debt, are pari passu in right of payment with any of their future senior subordinated debt and are senior in right of payment to any of their future subordinated debt. Operating's existing domestic subsidiaries, other than non-guarantor subsidiaries, are guarantors of the 9³/₄% senior subordinated notes. The 9³/₄% senior subordinated notes are secured by the assets of Operating and certain subsidiaries of Operating and by Operating's common stock owned by

Intermediate and such security interest is junior in priority to that securing first-lien obligations, including those under the Amended Wachovia Credit Facility.

Interest on the notes accrues at the rate of $9\frac{3}{4}\%$ per annum and is payable semi-annually in arrears on each June 23 and December 23. The notes mature on December 23, 2014. The notes may be redeemed at the option of the issuer, in whole or in part, at 101% of the principal amount at any time until June 23, 2006 and thereafter, at any time on or after December 23, 2009 at prices ranging from 104.875% to 100% of the principal amount, in each case, plus accrued and unpaid interest on the notes.

The indenture governing the $9\frac{3}{4}\%$ senior subordinated notes contains covenants that, among other things, limit the ability of Operating and certain subsidiaries of Operating to incur additional indebtedness or issue disqualified stock or preferred stock, pay dividends or make other distributions on, redeem or repurchase the capital stock of Operating, make certain investments, create certain liens, guarantee indebtedness, engage in transactions with affiliates and consolidate, merge or transfer all or substantially all of the assets of Operating and certain subsidiaries of Operating.

Under the indenture governing the $9\frac{3}{4}\%$ senior subordinated notes, Operating may declare cash dividends payable to Group in an amount sufficient to enable Group to make the regularly scheduled payment of interest in respect of the senior discount debentures of Group so long as no default or event of default has occurred and is continuing under the indenture. The ability of Operating to declare dividends on its capital stock is also limited by Delaware law, which permits a company to pay dividends on its capital stock only out of its surplus or, in the even that it has no surplus, out of its net profits for the year in which a dividend is declared or for the immediately preceding fiscal year. In order to pay dividends in cash, Operating must have surplus or net profits equal to the full amount of the cash dividend at the time such dividend is declared. In determining Operating's ability to pay dividends, Delaware law permits the board of directors of Operating to revalue its assets and liabilities from time to time to their fair market value in order to create a surplus.

(b) On February 4, 2003, Group and Operating entered into a credit agreement with TPG-MD Investment, LLC, a related party, which provides for a Tranche A loan to Operating in an aggregate principal amount of \$10.0 million and a Tranche B loan to Operating in an aggregate principal amount of \$10.0 million. The loans are due in February 2008 and bear interest at 5.0% per annum payable semi-annually in arrears on January 31 and July 31, commencing on July 31, 2003. Interest will compound and be capitalized and added to the principal amount on each interest payment date, resulting in an effective interest rate of 5.6%. The outstanding amount of these loans is convertible into shares of common stock of Group at \$6.82 per share. These loans are subordinated in right of payment to the prior payment of all senior debt. On November 21, 2004, this credit agreement was amended to subordinate the Tranche A loan in right of payment to Operating's $9\frac{3}{4}\%$ senior subordinated notes while the Tranche B loan is pari passu in right of payment with such notes.

(c) The $10\frac{3}{8}\%$ senior subordinated notes were redeemed in full in December 2004.

(d) On May 6, 2003, Group completed an offer to exchange 16% senior discount contingent principal notes due 2008 of Intermediate (new notes) for its outstanding 13¹/₈% senior discount debentures due 2008 (existing debentures). Approximately 85% of the outstanding debentures were tendered for exchange. Group exchanged \$87,006 fair value of new notes for \$131,083 face amount (including accrued interest of \$10,750) of existing debentures. The difference between the fair value of the new notes and the carrying value of the existing debentures of \$44,077 was included as a gain in the statement of operations for the year ended January 31, 2004.

The outstanding 16% senior discount contingent principal notes were redeemed in full through two separate redemption events in December 2004 and January 2005.

(e) The 13¹/₈% senior discount debentures are senior unsecured obligations of Group and mature on October 15, 2008. Interest is payable in arrears on April 15 and October 15 of each year subsequent to October 15, 2002. The 13¹/₈% senior discount debentures may be redeemed at the option of Group at 1.0219 of principal until October 15, 2005 and 100% thereafter.

(f) The restated certificate of incorporation authorizes Group to issue up to:

- (1) 1,000,000 shares of Series A cumulative preferred stock; par value \$.01 per share; and
- (2) 1,000,000 shares of Series B cumulative preferred stock; par value \$.01 per share.

At January 29, 2005 and January 31, 2004, 92,800 shares of Series A preferred stock and 32,500 shares of Series B preferred stock were issued and outstanding.

Each series of the preferred stock accumulates dividends at the rate of 14.5% per annum (payable quarterly) for periods ending on or prior to October 17, 2009. Dividends compound to the extent not paid in cash. A default in the payment of the Series A preferred stock redemption price will trigger dividends accruing and compounding quarterly at a rate of (i) 16.50% per annum with respect to periods ending on or before October 17, 2009 and (ii) 18.50% with respect to periods starting after October 17, 2009. A default in the payment of the Series B preferred stock redemption price will trigger dividends accruing and compounding quarterly at a rate of 16.50% per annum.

On October 17, 2009, Group is required to redeem the Series B preferred stock and to pay all accumulated but unpaid dividends on the Series A preferred stock. Thereafter, the Series A preferred stock will accumulate dividends at the rate of 16.5% per annum. Subject to restrictions imposed by certain indebtedness of the Company, Group may redeem shares of the preferred stock at a redemption price equal to 100% of liquidation value plus accumulated and unpaid dividends.

In certain circumstances (including a change of control of Group), subject to restrictions imposed by certain indebtedness of the Company, Group may be required to repurchase shares of the preferred stock at liquidation value plus accumulated and unpaid dividends. If Group liquidates, dissolves or winds up, whether voluntary or involuntary, no distribution shall be made either (i) to those holders of stock ranking junior to the preferred stock, unless prior thereto the holders of the preferred stock receive the total value for each share of preferred stock plus an amount equal to all accrued dividends thereon as of the date of such payment or (ii) to the holders of stock ranking *pari passu* with the

preferred stock (which we refer to as the "parity stock"), except distributions made ratably on the preferred stock and all such parity stock in proportion to the total amounts to which the holders of all such shares are entitled upon liquidation, dissolution or winding up of Group.

Effective at the beginning of the third quarter of 2003, the Company adopted SFAS No. 150 "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity". This pronouncement required the reclassification to long term debt of the liquidation value of Group Series B preferred stock and the related accumulated and unpaid dividends and the accumulated and unpaid dividends related to the Series A preferred stock since these amounts are required to be redeemed in October 2009. The preferred dividends related to the liquidation value of the Series B preferred stock and to the accumulated and unpaid dividends of the Series A and Series B preferred stock for the third and fourth quarters of 2003 and fiscal 2004 are included in interest expense. The Series A preferred stock is only redeemable in certain circumstances (including a change of control at Group) and does not qualify for reclassification under SFAS No. 150. Accordingly, the dividends related to the Series A preferred stock are deducted from stockholders' deficit.

Accumulated but unpaid dividends amounted to \$225,766 at January 29, 2005.

8. Gain (loss) on Refinancing of Debt

During the fourth quarter of 2004, the Company redeemed in full the outstanding 10³/₈% senior subordinated notes due 2007 (\$150.0 million) and redeemed the outstanding 16% senior discount contingent principal notes due 2008 (\$169.1 million). Funds used for the redemption were generated from the proceeds of a \$275 million term loan and internally available funds.

This refinancing resulted in a loss of \$49.8 million for Group in fiscal 2004, which consisted of: (a) redemption premiums of \$15.3 million, (b) the write-off of deferred financing costs of \$3.2 million and (c) the write-off of deferred debt issuance costs of \$31.3 million related to the 16% senior discount contingent principal notes issued in May 2003.

The loss on refinancing of debt for Operating in fiscal 2004 was \$4.0 million consisting of redemption premiums of \$2.6 million and the write off of deferred financing costs of \$1.4 million.

Refer to Note 7(d) for explanation of gain on exchange of debt in fiscal 2003.

9. Common Stock

The restated certificate of incorporation authorizes Group to issue up to 100,000,000 shares of common stock; par value \$.01 per share. At January 29, 2005, shares issued were 13,780,175 and shares outstanding were 13,207,086. At January 31, 2004, shares issued were 13,584,175 and shares outstanding were 13,011,086.

10. Commitments and Contingencies

(a) Operating Leases

As of January 29, 2005, Operating was obligated under various long-term operating leases for retail and factory outlet stores, warehouses, office space and equipment requiring minimum annual rentals.

These operating leases expire on varying dates through 2014. At January 29, 2005 aggregate minimum rentals are, as follows:

Fiscal year	Amount
2005	\$ 54,257
2006	50,636
2007	48,713
2008	43,115
2009	37,841
Thereafter	98,772

Certain of these leases include renewal options and escalation clauses and provide for contingent rentals based upon sales and require the lessee to pay taxes, insurance and other occupancy costs.

Rent expense for fiscal 2004, 2003 and 2002 was \$46,583, \$42,997 and \$41,657, respectively, including contingent rent, based on store sales, of \$1,700, \$814 and \$1,187.

(b) Employment Agreements

The Company is party to employment agreements with certain executives, which provide for compensation and certain other benefits. The agreements also provide for severance payments under certain circumstances.

(c) Litigation

The Company is subject to various legal proceedings and claims that arise in the ordinary conduct of its business. Although the outcome of these claims cannot be predicted with certainty, management does not believe that it is reasonably possible that resolution of these legal proceedings will result in unaccrued losses that would be material.

11. Employee Benefit Plan

The Company has a thrift/savings plan pursuant to Section 401 of the Internal Revenue Code whereby all eligible employees may contribute up to 15% of their annual base salaries subject to certain limitations. The Company's contribution is based on a percentage formula set forth in the plan agreement. Company contributions to the thrift/savings plan were \$1,306, \$1,288 and \$1,834 for fiscal 2004, 2003 and 2002, respectively.

12. License Agreement

Operating has a licensing agreement through January 2007 with Itochu Corporation, a Japanese trading company. The agreement permits Itochu to distribute J.Crew merchandise in Japan.

Operating earns royalty payments under the agreement based on the sales of its merchandise. Royalty income, which is included in other revenues, for fiscal 2004, 2003, and 2002 was \$2,757, \$2,456 and \$2,280, respectively.

13. Other Revenues

Other revenues consist of the following:

	2004	2003	2002
Shipping and handling fees	\$ 21,624	\$ 25,205	\$ 31,823
Royalties	2,757	2,456	2,280
Other	1,540	1,676	1,962
	<u>\$ 25,921</u>	<u>\$ 29,337</u>	<u>\$ 36,065</u>

14. Financial Instruments

The fair value of the Company's long-term debt (including redeemable preferred stock) is estimated to be approximately \$576,933 and \$501,400 at January 29, 2005 and January 31, 2004, respectively, and is based on dealer quotes or quoted market prices of the same or similar instruments. The carrying amounts of long-term debt were \$576,933 and \$517,804 at January 29, 2005 and January 31, 2004, respectively. The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts payable and other current liabilities approximate fair value because of the short-term maturity of those financial instruments. The estimates presented herein are not necessarily indicative of amounts the Company could realize in a current market exchange.

15. Income Taxes

Group files a consolidated federal tax return, which includes all its wholly owned subsidiaries. Each subsidiary files separate state tax returns in the required jurisdictions. Group and its subsidiaries have entered into a tax sharing agreement providing (among other things) that each of the subsidiaries will reimburse Group for its share of income taxes based on the proportion of such subsidiaries' tax liability on a separate return basis to the total tax liability of Group.

The income tax provision/(benefit) of Group consists of:

	2004	2003	2002
Current:			
Foreign	\$ 300	\$ 250	\$ 193
Federal	—	(3,744)	(12,014)
State and local	300	(1,006)	200
	600	(4,500)	(11,621)
Deferred	—	5,000	7,421
Total	\$ 600	\$ 500	\$ (4,200)

A reconciliation between the provision/(benefit) for income taxes based on the U.S. Federal statutory rate and the Company's effective rate, is as follows:

	2004	2003	2002
Federal income tax rate	(35.0)%	(35.0)%	(35.0)%
State and local income taxes, net of federal benefit	0.4	0.8	—
Valuation allowance	5.6	64.0	47.0
Additional NOL carryback	—	(7.4)	—
Reversal of prior tax accruals	—	(2.6)	(20.9)
Non-deductible expenses and other (primarily preferred dividends)	18.6	8.4	(.5)
Non-recognized gain on exchange of debt	11.0	(27.2)	—
Effective tax rate	0.6 %	1.0 %	(9.4)%

The tax effect of temporary differences which give rise to deferred tax assets and liabilities are:

	January 29, 2005	January 31, 2004
Deferred tax assets:		
Original issue discount	\$ 3,600	\$ 33,660
Rent	17,800	17,514
Federal NOL carryforwards	47,200	19,600
State and local NOL carryforwards	4,500	4,485
Reserve for sales returns	1,900	1,207
Other	4,700	5,057
	<u>79,700</u>	<u>81,523</u>
Valuation allowance	(63,400)	(57,838)
	<u>16,300</u>	<u>23,685</u>
Deferred tax liabilities:		
Prepaid catalog and other prepaid expenses	(6,600)	(8,555)
Difference in book and tax basis for property and equipment	(9,700)	(15,130)
	<u>(16,300)</u>	<u>(23,685)</u>
Net deferred income tax asset	<u>\$ —</u>	<u>\$ —</u>

Operating

The income tax provision/(benefit) of Operating consists of:

	2004	2003	2002
Current:			
Foreign	\$ 300	\$ 250	\$ 193
Federal	—	(3,744)	(13,449)
State and local	300	(1,006)	200
	<u>600</u>	<u>(4,500)</u>	<u>(13,056)</u>
Deferred	—	(910)	(4,694)
Total	<u>\$ 600</u>	<u>\$ (5,410)</u>	<u>\$ (17,750)</u>

A reconciliation between the provision/(benefit) for income taxes based on the U.S. Federal statutory rate and the Company's effective rate is as follows:

	2004	2003	2002
Federal income tax rate	35.0%	(35.0)%	(35.0)%
State and local income taxes, net of federal benefit	3.4	0.8	—
Valuation allowance	(32.3)	36.9	—
Additional NOL carryback	—	(7.8)	—
Reversal of prior tax accruals	—	(2.7)	(38.6)
Non-deductible expenses and other	(.9)	(3.6)	6.8
Effective tax rate	5.2%	(11.4)%	(66.8)%

The tax effect of temporary differences which give rise to deferred tax assets and liabilities are:

	January 29, 2005	January 31, 2004
Deferred tax assets:		
Federal NOL carryforwards	\$ 6,200	\$ 17,540
State and local NOL carryforwards	4,500	4,485
Reserve for sales returns	1,900	1,207
Rent	17,800	17,514
Other	4,700	5,459
	35,100	46,205
Valuation allowance	(18,800)	(22,520)
	16,300	23,685
Deferred tax liabilities:		
Prepaid catalog and other prepaid expenses	(6,600)	(8,555)
Difference in book and tax basis for property and equipment	(9,700)	(15,130)
	(16,300)	(23,685)
Net deferred income tax asset	\$ —	\$ —

The Company has significant deferred tax assets resulting from net operating loss carryforwards and deductible temporary differences, which will reduce taxable income in future periods. SFAS No. 109 "Accounting for Income Taxes" states that a valuation allowance is required when it is more likely than not that all or a portion of a deferred tax asset will not be realized. A review of all available positive and negative evidence needs to be considered, including a company's current and past performance, the market environment in which a company operates, length of carryback and carryforward periods, existing contracts or sales backlog that will result in future profits, etc. Forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as

cumulative losses in recent years. Cumulative losses weigh heavily in the overall assessment. As a result of our assessment, we established a valuation allowance for the net deferred tax assets at February 1, 2003. The valuation allowance was increased at January 31, 2004 and January 29, 2005 to fully reserve net deferred tax assets at such dates. The Company did not recognize any tax benefits in fiscal 2004 and does not expect to recognize any tax benefits in future results of operations until an appropriate level of profitability is sustained.

The Company has state and local income tax net operating loss carryforwards of varying amounts.

16. Stock Compensation Plans

Amended and Restated 1997 Stock Option Plan

Under the terms of the Amended and Restated 1997 Stock Option Plan (1997 Plan), an aggregate of 1,910,000 shares of Group common stock are available for grant to key employees and consultants in the form of non-qualified stock options. The options have terms of seven to ten years and become exercisable over a period of four to five years. Options granted under the 1997 Plan are subject to various conditions, including under some circumstances, the achievement of certain performance objectives.

2003 Equity Incentive Plan

In January 2003, the Board of Directors of Group approved the adoption of the 2003 Equity Incentive Plan (2003 Plan). Under the terms of the 2003 Plan, an aggregate of 4,798,160 shares of Group common stock are available for award to key employees and consultants in the form of non-qualified stock options and restricted shares, as follows:

- 1,115,812 shares are reserved for the issuance of stock options at an exercise price of \$6.82 or fair market value, whichever is greater;
- 1,115,812 shares are reserved for the issuance of stock options at an exercise price of \$25.00 or fair market value, whichever is greater;
- 1,115,812 shares are reserved for the issuance of stock options at an exercise price of \$35.00 or fair market value, whichever is greater;
- 1,450,724 shares are reserved for the issuance of restricted shares.

The options have terms of ten years and become exercisable over the period provided in each grant agreement. Under the Plan, the Compensation Committee of the Board of Directors of Group has the discretion to modify the exercise price and the number of shares reserved for the issuance of stock options and restricted shares.

A summary of stock option activity for the three years ended January 29, 2005, is as follows:

	2004		2003		2002	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding, beginning of year	2,410,606	\$ 8.37	4,474,469	\$ 18.22	1,808,790	\$ 9.97
Granted	2,515,848	17.07	377,750	6.85	3,263,239	21.35
Exercised	—	—	—	—	—	—
Cancelled	(344,189)	8.33	(2,441,613)	26.19	(597,560)	10.29
Outstanding, end of year	4,582,265	\$ 13.15	2,410,606	\$ 8.37	4,474,469	\$ 18.22
Options exercisable at end of year	1,508,850	\$ 9.84	849,302	\$ 10.59	842,340	\$ 9.81

The following table summarizes information about stock options outstanding as of January 29, 2005:

Range	Outstanding			Exercisable	
	Number of options	Weighted average option price	Weighted average remaining contractual life (in months)	Number of options	Weighted average option price
\$6.82–\$8.53	2,131,731	\$ 6.85	86	777,723	\$ 6.82
\$10.00–\$35.00	2,450,534	18.62	88	731,127	13.06
\$6.82–\$35.00	4,582,265	\$ 13.15	87	1,508,850	\$ 9.84

Under the 2003 Plan, 1,004,266, 224,402 and 196,000 restricted shares were issued in fiscal 2002, 2003 and 2004, respectively, and 83,689 restricted shares were forfeited in fiscal 2003. On January 29, 2005, there were 1,340,979 restricted shares outstanding, of which 509,979 shares were vested.

17. Recent Accounting Pronouncements

In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. FIN 46R applies to variable interests in variable interest entities created after December 31, 2003. For variable interests in variable interest entities created before January 1, 2004, the Interpretation applies beginning on January 1, 2005. For any variable interest entities that must be consolidated under FIN 46R that were created before January 1, 2004, the assets, liabilities and noncontrolling interests of the variable interest entity initially would be measured at their carrying amounts with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting

change. If determining the carrying amounts is not practicable, fair value at the date FIN 46R first applies may be used to measure the assets, liabilities and noncontrolling interest of the variable interest entity. The adoption of FIN 46R did not have any effect on the financial statements taken as a whole as of January 29, 2005, and for the year then ended.

In December 2004, the FASB issued Statement No. 123 R, *Share-Based Payment*. This revision to Statement No. 123 requires that compensation expense be recognized for the fair value of stock options over their vesting period and changes the method of expense recognition for performance-based stock awards. The Statement is required to be adopted by the Company for fiscal years beginning after December 15, 2005 and applies to all outstanding stock options and stock awards that have not yet vested at the date of adoption. Management is evaluating the effects of this Statement.

18. Quarterly Financial Information (Unaudited)

	13 weeks ended 5/3/03	13 weeks ended 8/2/03(a)	13 weeks ended 11/1/03	13 weeks ended 1/31/04	52 weeks ended 1/31/04
	(\$ in millions)				
Net sales	\$ 152.6	\$ 159.2	\$ 146.4	\$ 202.4	\$ 660.6
Gross profit	57.9	51.3	59.9	80.6	249.7
Net income/(loss)—Group	(20.2)	15.0	(24.5)	(20.5)	(50.2)
Net income/(loss)—Operating	(15.5)	(18.0)	(9.2)	.7	(42.0)
	13 weeks ended 5/1/04	13 weeks ended 7/31/04	13 weeks ended 10/30/04	13 weeks ended 1/29/2005(b)	52 weeks ended 1/29/05
Net sales	\$ 140.6	\$ 182.1	\$ 200.9	\$ 254.7	\$ 778.3
Gross profit	60.7	74.2	89.0	101.5	325.4
Net loss—Group	(23.7)	(13.8)	(9.9)	(52.9)	(100.3)
Net income/(loss)—Operating	(7.7)	3.2	7.5	8.4	11.4

(a) Net income of Group includes a pre-tax gain on the exchange of debt of \$41.1 million.

(b) Net loss of Group includes a pre-tax loss on the refinancing of debt of \$49.8 million and net income of Operating includes a pre-tax loss of \$4.0 million related to the refinancing of debt.

SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS

	beginning balance		charged to cost and expenses(a)		charged to other accounts		deductions(a)		ending balance
					(in thousands)				
<i>Inventory reserve</i>									
(deducted from inventories)									
Fiscal year ended:									
February 1, 2003	\$	8,367	\$	4,053	\$	—	\$	—	\$ 12,420
January 31, 2004		12,420		—		—		7,380	5,040
January 29, 2005		5,040		—		—		557	4,483
<i>Allowance for sales returns</i>									
(included in other current liabilities)									
Fiscal year ended:									
February 1, 2003	\$	6,475	\$	—	\$	—	\$	1,162	\$ 5,313
January 31, 2004		5,313		—		—		2,309	3,004
January 29, 2005		3,004		1,827		—		—	4,831

- (a) The inventory reserve and allowance for sales returns are evaluated at the end of each fiscal quarter and adjusted (plus or minus) based on the quarterly evaluation. During each period inventory write-downs and sales returns are charged to the statement of operations as incurred.

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[SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS](#)

September 15, 2003

Roxane Al-Fayez
[address omitted]

Dear Roxane,

We are pleased to extend an offer to join our team as Executive Vice President of Direct Operations, reporting to Millard S. Drexler.

We will provide you with professional challenges, education and ongoing support as you continue your career with J.Crew. Your compensation will include a base salary of \$375,000 annualized (\$14,423.08 biweekly), payable in accordance with J.Crew's normal payroll practices. In addition, our competitive benefits package includes the following:

30 paid time off days each subsequent fiscal year (beginning February 2004)
medical, vision & dental insurance
short & long term disability
life insurance and long term care
401(k) tax deferred savings plan (after 1 year with us)
tax deferred flexible spending accounts for health, dependent care & commutation
tuition reimbursement
30 percent merchandise discount (in stores, online & through the catalog)

You will be eligible to receive a \$50,000 sign-on bonus payable two weeks after your start date. All bonus payments are subject to applicable tax withholdings and are contingent upon you being an active associate on the date of actual disbursement. If you voluntarily terminate your employment for any reason within one year after your start date, you agree to repay to the Company a prorated amount of this bonus based on your last date of active employment. You must repay this amount within thirty days thereafter of your last date of active employment.

For fiscal year 2003, we will pay you a minimum guaranteed bonus equal to \$50,000 payable April, 2004. For fiscal year 2003 and beyond, you will be eligible to receive an annual bonus under the company's bonus plan based upon a range of 25% - 100% of your annual base salary, with a target of 50%. Bonus payments are conditioned upon the company's achievement of certain performance objectives and your individual performance and are pro-rated based upon date of hire. It is company policy to make bonus payments after the close of our fiscal year, usually mid-April, and all bonus payments are subject to applicable tax withholdings and are contingent upon you being an active associate on the date of actual disbursement.

In addition, you will receive a \$25,000 bonus payment payable in October of 2004. All bonus payments are subject to applicable tax withholdings and are contingent upon you being an active associate on the date of actual disbursement.

You will be eligible to participate in our Stock Option Plan. Subject to approval of the provisions set forth in the Plan and your Stock Option Grant Agreement, the Company will grant to you a non-qualified stock option to purchase 35,000 shares of J.Crew Group, Inc. Common Stock. The Stock Option Grant Agreement will provide the exercise price, vesting schedule, expiration and other relevant terms.

You will also receive a grant of 25,000 restricted shares of Common Stock. The terms and conditions, including the vesting schedule, of the Restricted Shares shall be evidenced by a separate Restricted Stock Agreement.

J.Crew will provide you with a monthly housing allowance of \$3,000 for as long as you are an active employee. You will be notified through our Relocation Services to aid you in this process. If your employment is terminated by us for reasons other than cause prior to the earlier of (1) 12 months after

the effective date of your housing lease or (2) 18 months after your start date with us, J.Crew will continue to reimburse you for your actual monthly rental payments up to \$3,000 per month for the remaining term of your 12-month lease (the "Remaining Term"). In the event that you sublease, transfer or terminate your lease anytime during the Remaining Term, J. Crew's obligations to reimburse you as set forth herein shall terminate immediately.

You represent to J.Crew that you do not have any other agreements, arrangements or commitments with any other person or entity that conflict with accepting this offer or performing your obligations and that you will not disclose to J.Crew or use any proprietary information or trade secrets of another person or entity. You also agree that you will keep all proprietary, confidential information of J.Crew strictly confidential and not disclose any such information during or after your employment without J.Crew's prior written consent, and that you will abide by all J.Crew policies, including, but not limited to, those contained in the Code of Ethics and Business Practices.

Through the interview process we had the chance to get to know each other. We know that you will add value to our team and hope that you decide to join the crew. While we believe that this will be a mutually beneficial relationship, your employment is "at will" and may be terminated by you or the Company at any time. This offer is contingent upon the successful completion of a background screen and reference check.

If you agree that J.Crew and this offer are right for you, kindly sign a copy of this letter and fax it to my attention at [fax number omitted] or mail it to the address below. Please do not hesitate to contact me by phone [phone number omitted] or email [email address omitted] if you have any questions or require additional information.

We look forward to hearing from you soon.

Regards,

Agreed to and Accepted:		
/s/ MILLARD S. DREXLER	/s/ ROXANE AL-FAYEZ	9/15/03
Millard S. Drexler Chief Executive Officer 770 Broadway NY, NY 10003	Roxane Al-Fayez	Date

January 5, 2004

Roxane Al-Fayez
[address omitted]

Dear Roxane,

This is an addendum to your offer letter of September 15, 2003.

J.Crew will reimburse you or your husband for weekly commutation to and from your principal residence in Ohio for the term of your employment with the company.

Agreed to and Accepted:

/s/ LYNDA MARKOE	1/6/04
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Lynda Markoe VP, Human Resources	Date
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/s/ ROXANE AL-FAYEZ	1/6/04
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Roxane Al-Fayez Date EVP, Direct Operations	Date
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[EXHIBIT 10.16](#)

October 7, 2004

Mr. Paul Fusco
[address omitted]

Dear Paul:

This letter will confirm our understanding of the arrangements under which your employment with the Company is terminated. The terms and conditions of the termination of your employment with the Company are set out below.

1. The parties hereby acknowledge and confirm that your employment with the Company is terminated effective as of October 22, 2004 (the "*Termination Date*").
 2. Subject to this Agreement becoming effective (as described in Paragraph 18 hereof), the Company will continue to pay you your base salary of \$275,000 per annum for the twelve (12) month period beginning on the day immediately following the Termination Date ("*Severance Period*"), payable in accordance with the Company's regular payroll practices for its employees. You will also continue to have medical coverage during the Severance Period on the same terms and conditions as medical coverage is then made available to the employees of the Company. The foregoing payments shall be reduced by any required tax withholdings and shall not be taken into account as compensation and no service credit shall be given after the Termination Date for purposes of determining the benefits payable under any other plan, program, agreement or arrangement of the Company. You acknowledge that, except for the foregoing payments, you are not entitled to any payment by the Company in the nature of either severance or termination pay or other compensation of any kind.
 3. As of the Termination Date, you have vested options to purchase 3,200 shares of Common Stock ("*Common Stock*") of J. Crew Group, Inc. ("*Parent*") at \$10.00 per share, 8,800 shares of Common Stock at \$11.00 per share, 3,000 shares of Common Stock at \$19.18 per share, 4,000 shares of Common Stock at \$10.65 per share and 3,750 shares of Common Stock at \$6.82 per share (collectively, the "*Vested Options*"). In addition, you have unvested options to purchase 800 shares of Common Stock at \$10.00 per share, 2,200 shares of Common Stock at \$11.00 per share, 2,000 shares of Common Stock at \$19.18 per share, 6,000 shares of Common Stock at \$10.65 per share and 16,250 shares of Common Stock at \$6.82 per share (collectively, the "*Unvested Options*"). You acknowledge that all of the Vested Options will terminate 90 days after the Termination Date and that all of the Unvested Options terminate effective immediately, in accordance with the provisions of your stock option agreements with Parent and the J. Crew Group, Inc. 1997 Stock Option Plan, as amended (the "*Option Plan*"). All of the shares of Common Stock that may be acquired by you pursuant to your vested options shall be subject to the Stockholders' Agreement attached to the Option Plan as Exhibit B.
 4. By signing this Agreement, you agree that in exchange for the consideration set forth herein, you hereby voluntarily, fully and unconditionally release and forever discharge the Company, Parent, their present and former parent corporation(s), subsidiaries, divisions, affiliates and otherwise related entities and their respective incumbent and former employees, directors, plan administrators, officers and agents, individually and in their official capacities (collectively, the "*Releasees*"), from any and all charges, actions, causes of action, demands, debts, dues, bonds, accounts, covenants, contracts, liabilities, or damages of any nature whatsoever, whether now known or claimed, to whomever made, which you have or may have against any or all of the Releasees for or by reason of any cause, nature or thing whatsoever, up to the present time, arising out of or related to your employment with the Company or the termination of such employment, including, by way of examples and without limiting the broadest application of the foregoing, any actions, causes of action, or claims under any contract or federal, state or local decisional law, statutes, regulations or constitutions, any claims for notice, pay in lieu of notice,
-

wrongful dismissal, breach of contract, defamation or other tortious conduct, discrimination on the basis of actual or perceived disability, age, sex, race or any other factor (including, without limitation, any claim pursuant to Title VII of the Civil Rights Act of 1964, Americans with Disabilities Act of 1990, the Age Discrimination in Employment Act of 1967, as amended, the Family and Medical Act of 1993, the Equal Pay Act of 1963, the Fair Labor Standards Act, the State, City and local laws of New York, and the equal employment law or laws of the state and/or city in which you work), any claim pursuant to any other applicable employment standards or human rights legislation or for severance pay, salary, bonus, incentive or additional compensation, vacation pay, insurance, other benefits, interest, and/or attorney's fees. You acknowledge that this general release is not made in connection with an exit incentive or other employment termination program offered to a group or class of employees.

If you have made or should hereafter make any complaint, charge, claim, allegation or demand, or commence or threaten to commence any action, complaint, charge, claim or proceeding, against any or all of the Releasees for or by reason of any cause, matter or thing whatsoever existing up to the present time, this Agreement may be raised as and shall constitute a complete bar to any such action, complaint, charge, claim, allegation or proceeding, and, subject to a favorable ruling by a tribunal of final jurisdiction, the Releasees shall recover from you, and you shall pay to the Releasees, all costs incurred by them, including their attorneys' fees, as a consequence of any such action, complaint charge, claim, allegation or proceeding; provided, however, that this shall not limit you from enforcing your rights under this Agreement, and in the event any action is commenced to enforce your rights under this Agreement, each party shall bear its own legal fees and expenses; and provided further, however, that this is not intended to interfere with your right to file a charge with the Equal Employment Opportunity Commission ("EEOC") in connection with any claim you believe you may have against any Releasee. However, by signing this Agreement, you agree to waive any right to recover in any proceeding you may bring before the EEOC (or any state human rights commission) or in any proceeding brought by the EEOC (or any state human rights commission) on your behalf.

You specifically release all claims under the Age Discrimination in Employment Act ("ADEA") relating to your employment and its termination.

5. You acknowledge that the payments described in Section 2 above that you are receiving in connection with the foregoing release are in accordance with your letter agreement, dated June 18, 2001 ("*Letter Agreement*").
6. You hereby agree and acknowledge that you shall be bound by and comply with the restrictive covenants provided in Section 3 of the Letter Agreement (the "*Restrictive Covenants*"), and that such Restrictive Covenants are hereby made part of this Agreement as if specifically restated herein and that the payments described in Section 2 above that you are receiving are subject to and contingent upon your compliance with Restrictive Covenants. You also agree to be available to answer any questions and otherwise cooperate with the Company as reasonable during the Severance Period to assist in any necessary transitions.
7. You acknowledge and agree that, notwithstanding any other provision of this Agreement, if you breach any of your obligations under this Agreement or any Restrictive Covenant, (a) you will forfeit your right to receive the payments and benefits described in Section 2 above (to the extent the payments were not theretofore paid) and the Company shall be entitled to recover any payments already made to you or on your behalf, (b) the Vested Options shall expire as of the date of such breach to the extent not theretofore exercised and, if exercised as of the date of such breach, you shall immediately reimburse the Company for the profit upon exercise (such profit calculated as the difference between the (i) greater of either the Fair Market Value (as defined in the Option Plan) of a share of Common Stock on the date of exercise or the amount paid by the

Company to you per share of Common Stock for the purchase of the shares acquired upon exercise, and (ii) exercise price, times the number of options exercised).

8. You hereby agree that the breach of any Restrictive Covenant may cause the Company to suffer irreparable harm for which money damages would not be an adequate remedy and therefore, if you breach a Restrictive Covenant, the Company would be entitled to temporary and permanent injunctive relief in any court of competent jurisdiction (without the need to post any bond) without prejudice to any other remedies under this Agreement or otherwise.
9. You agree that, in the event that you are served with legal process or other request purporting to require you to testify, plead, respond or defend and/or produce documents at a legal proceeding, threatened proceeding, investigation or inquiry involving the Releasees, you will: (1) refuse to provide testimony or documents absent a subpoena, court order or similar process from a regulatory agency; (2) within three (3) business days or as soon thereafter as practical, provide oral notification to the Company's General Counsel of your receipt of such process or request to testify or produce documents; and (3) provide to the Company's General Counsel by overnight delivery service a copy of all legal papers and documents served upon you. You further agree that in the event you are served with such process, you will meet and confer with the Company's designee(s) in advance of giving such testimony or information. You also agree to cooperate fully with the Releasees in connection with any existing or future litigation against the Releasees, whether administrative, civil or criminal in nature, in which and to the extent the Releasees deem your cooperation necessary. The Company agrees to reimburse you for your reasonable out-of-pocket expenses incurred in connection with the performance of your obligations under this Section 9.
10. This Agreement does not constitute an admission of liability or wrongdoing of any kind by you or the Company or its affiliates.
11. The terms of this Agreement shall be binding on the parties hereto and their respective successors, assigns, heirs and representatives.
12. This Agreement, together with your stock option agreements with Parent and the Option Plan, constitute the entire understanding of the Company and you with respect to the subject matter hereof and supersedes all prior understandings, written or oral. The terms of this Agreement may be changed, modified or discharged only by an instrument in writing signed by the parties hereto. A failure of the Company or you to insist on strict compliance with any provision of this Agreement shall not be deemed a waiver of such provision or any other provision hereof. If any provision of this Agreement is determined to be so broad as to be unenforceable, such provision shall be interpreted to be only so broad as is enforceable.
13. This Agreement shall be construed, enforced and interpreted in accordance with and governed by the laws of the State of New York.
14. The parties hereto acknowledge and agree that each party has reviewed and negotiated the terms and provisions of this Agreement and has contributed to its revision. Accordingly, the rule of construction to the effect that ambiguities are resolved against the drafting party shall not be employed in the interpretation of this Agreement. Rather, the terms of this Agreement shall be construed fairly as to both parties hereto and not in favor or against either party.
15. This Agreement may be executed in any number of counterparts and by different parties on separate counterparts, each of which counterpart, when so executed and delivered, shall be deemed to be an original and all of which counterparts, taken together, shall constitute but one and the same Agreement.
16. You acknowledge that, by your free and voluntary act of signing below, you agree to all of the terms of this Agreement and intend to be legally bound thereby.

17. You acknowledge that you have received this Agreement on or before October 7, 2004. You understand that you may consider whether to agree to the terms contained herein for a period of twenty-one (21) days after the date hereof. However, the operation of the provisions of Sections 2 through 4 above may be delayed until you execute this Agreement and return it to the Company and it becomes effective as provided below. You acknowledge that you have consulted with an attorney prior to your execution of this Agreement or have determined by your own free will not to consult with an attorney.
18. This Agreement will become effective, enforceable and irrevocable seven days after the date on which it is executed by you (the "*Effective Date*"). During the seven-day period prior to the Effective Date, you may revoke your agreement to accept the terms hereof by indicating in writing to the Vice President of Human Resources your intention to revoke. If you exercise your right to revoke hereunder, you shall forfeit your right to receive any of the payments and other benefits provided for herein, and to the extent such payments or benefits have already been made, you agree that you will immediately reimburse the Company for the value of such payments and benefits.

If the foregoing correctly reflects our understanding, please sign the enclosed copy of this letter agreement, whereupon it will become a binding agreement between us.

J. CREW OPERATING CORP.

By: /s/ Lynda Markoe

Lynda Markoe
Vice President
Human Resources

Agreed to and accepted:

By: /s/ Paul Fusco

Paul Fusco

Dated: 10/18, 2004

Acknowledgment

STATE OF New York)

ss:

COUNTY OF New York)

On the 18th day of October, 2004, before me personally came Paul Fusco who, being by me duly sworn, did depose and say that he resides at [address omitted], and did acknowledge and represent that he has had an opportunity to consult with attorneys and other advisers of his choosing regarding the Agreement set forth above, that he has reviewed all of the terms of the Agreement and that he fully understands all of its provisions, including without limitation, the general release and waiver set forth therein.

/s/ ROSEMARY RODRIGUEZ

Notary Public

Date: 10/18/04

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[EXHIBIT 10.17](#)

UNIVERSITY VILLAGE

LEASE AGREEMENT

THIS LEASE is made and entered into this 14th day of October, 2003 between UNIVERSITY VILLAGE LIMITED PARTNERSHIP, a Washington limited partnership ("Landlord"), whose address is 2673 Northeast University Village Mall, Suite 7, Seattle, Washington 98105, and GRACE HOLMES, INC., a Delaware corporation ("Tenant"), whose address is 770 Broadway, New York, NY 10003.

Landlord owns the real property and improvements located thereon as described in Subsection 2.1 ("University Village").

Landlord desires to lease certain space in University Village more particularly described on Exhibit D attached hereto and by this reference incorporated herein (the "Leased Premises") to Tenant and Tenant desires to take and lease such space from Landlord.

NOW THEREFORE, for and in consideration of the rents reserved hereunder, the terms and conditions hereof and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, Landlord hereby leases to Tenant and Tenant leases from Landlord, the Leased Premises upon the following terms and conditions:

1. LEASE TERMS AND EXHIBITS.

The following terms as used herein shall have the meanings set forth below unless specifically modified elsewhere in this Lease:

1.1 Leased Premises: That certain space in University Village known as Space "19" and more particularly described on Exhibit D attached hereto and by this reference incorporated herein.

1.2 Minimum Rent:

Years 1-5:	\$40.00 per square foot of the Area of Leased Premises per annum
Years 6-10:	\$44.00 per square foot of the Area of Leased Premises per annum

1.3 Lease Term: Ten (10) Lease Years plus a "partial year" (if any) from the Commencement Date to January 31 of the following year. The Lease Term shall commence as provided in Section 3 below, and shall end on the January 31 next following the 10th anniversary of the Commencement Date ("Expiration Date").

1.4 Area of Leased Premises: Approximately 7,400 square feet, consisting of 5,700 square feet on the ground level and 1,700 square feet of mezzanine space, and containing approximately 45 lineal feet of frontage. The exact size of the Leased Premises will be determined following remeasurement pursuant to Section 20.4 below.

1.5 Tenant's Fraction: A fraction, the numerator of which is the ground level portion of the Area of Leased Premises and the denominator of which is the sum of the numerators (gross leasable areas) used in all leases in University Village (whether or not leases are actually in effect for all of such space) in determining University Village Expenses payable by the tenants under such leases, provided the same shall include not less than 90% of the total leasable retail area in University Village.

1.6 Percentage Rent Rate: Five Percent (5%)

1.7 Percentage Rent Period: Lease Year.

1.8 Lease Year: The twelve month period ending each January 31 during the Lease Term.

1.9 Retail Trade Area: [none]

1.10 Security Deposit: [none]

1.11 Permitted Use: Tenant shall use the Leased Premises solely for the retail sale of men's, women's and children's ready-to-wear apparel, accessories, footwear, outerwear, related items sold under the J. Crew label, facial and body care products and home furnishings (the display of which shall not be more than 30% of the retail sales floor area), and for the retail sale of any other item featured in any catalogue offered by Tenant, its parent(s), affiliate(s) or subsidiary(ies) and any other item manufactured by or for Tenant, its parent(s), affiliate(s) or subsidiary(ies) provided such other item (i) is offered for sale in the majority of J. Crew retail stores, (ii) carries the J. Crew name/label and (iii) is complementary in nature to the J. Crew retail store at the time of the Commencement Date, and for no other purpose whatsoever.

1.12 Tenant's Trade Name: J. Crew

1.13 Name and Address of Tenant's Guarantor: [none]

1.14 Default Rate: The "Default Rate" is that rate of interest per annum equal to two percent (2%) over the prime rate of interest charged, quoted or published by Bank of America or its successor or, if Bank of America or its successor should fail to publish such information, by a comparable bank.

1.15 Exhibits: The Exhibits attached to this Lease are incorporated in this Lease by this reference. Each party agrees to perform any obligations on its part stated in any of such Exhibits:

Exhibit A.	Legal Description of University Village
Exhibit B.	Site Plan of University Village

Exhibit C.	Description of Landlord's and Tenant's Work
Exhibit D.	Plan of Leased Premises (which shall establish the floor area ("Floor Area") contained therein).
Exhibit 15.2	Similarly Situated Tenants

2. PREMISES.

2.1 University Village.

(a) **Definition.** Landlord is the owner of University Village, which is legally described in Exhibit A and depicted in the Site Plan of University Village attached hereto as Exhibit B. University Village shall include any adjacent property acquired by the Landlord from time to time during the term of this Lease, whether owned or leased by Landlord as a tenant under a ground lease or sublease, or which is otherwise operated on an integrated basis with University Village, whether or not the same is owned or controlled by Landlord.

(b) **No Representations.** The depiction of University Village in Exhibit B does not constitute a representation, covenant or warranty of any kind by Landlord, and subject to Section 13.2 below, Landlord reserves the right from time to time to change the size and dimensions of University Village; locate, relocate, alter and/or modify the number and location of buildings, building dimensions, the number of floors in any of the buildings, parking areas, driveways and entrances and exits to and from adjoining streets and ways, store dimensions, identity and type of other stores and tenancies and the common areas located from time to time in or on University Village. The term "University Village" as used herein shall refer to University Village described and depicted in Exhibits A and B, respectively, and as so changed, relocated, altered and/or modified. Landlord further agrees that it will make no change in the layout of the Leased Premises or University Village which will materially reduce the size, dimensions or usable area of the Leased Premises or materially adversely affect access to the Leased Premises. Landlord will make reasonable efforts to minimize the impact of any noise, dust, dirt and the like caused by Landlord's improvements or alterations on Tenant's business.

2.2 Leased Premises. Landlord hereby leases and demises to Tenant, and Tenant hereby accepts from Landlord, subject to and with the benefit of the terms and provisions of this Lease, the Leased Premises depicted in Exhibit D. The gross leasable area of the Leased Premises is as stated in Section 1.4 above.

3. TERM.

3.1 Lease Term. This Lease shall be for the term stated in Section 1.3 above (the "Term" or "Lease Term") and shall commence on the earlier of (a) one hundred twenty (120) days following the latest to occur of (i) Landlord's approval of Tenant's plans for Tenant's Work (defined below) provided Tenant submits plans for Tenant's Work to Landlord no later than November 1, 2003 and thereafter timely responds to comments from Landlord, (ii) Landlord's delivery of the

Leased Premises to Tenant in a broom clean condition, free of all violations and the personal property and signage of any previous occupant, with Substantial Completion of Landlord's Work (as defined in Section 3.2(a) below) and (iii) the date Tenant receives a building permit for the construction of Tenant's Work provided Tenant submits plans for Tenant's Work to the City of Seattle no later than December 1, 2003 and thereafter timely responds to comments from the City of Seattle or (b) the day that Tenant opens for business (the "Commencement Date"). It is anticipated that Landlord will deliver possession of the Leased Premises to Tenant on March 1, 2004 (the "Anticipated Delivery Date"), however, Landlord's failure to do so shall not result in any liability to Landlord or otherwise affect Tenant's obligations under this Lease except as otherwise set forth below. If for any reason Landlord is unable to deliver possession of the Leased Premises on the Anticipated Delivery Date, Landlord must provide written documentation to Tenant no later than forty-five (45) days prior to the Anticipated Delivery Date. If Landlord is unable to deliver possession of the Leased Premises on the Anticipated Delivery Date and Landlord fails to provide such notification to Tenant when required, then Landlord shall pay to Tenant, as liquidated damages, \$750.00 per day for each day of delay (the "Late Fee"). If such delay continues beyond July 1, 2004, then, in addition to any Late Fee that may be due Tenant, Tenant shall have the right to terminate this Lease upon notice to Landlord delivered no later than the earlier of (i) July 15, 2004 and (ii) the date of Landlord's Delivery of the Leased Premises to Tenant. In the event Tenant terminates this Lease in accordance with the preceding sentence, Landlord shall reimburse Tenant for the reasonable out-of-pocket costs incurred by Tenant in preparation and/or review of Tenant's plans and specifications for the Leased Premises. In no event shall Tenant be required to accept delivery of possession of the Leased Premises prior to the Anticipated Delivery Date.

Notwithstanding anything to the contrary contained herein, Tenant shall not be required to begin construction or initially open for business in the Leased Premises unless (a) tenants occupying ninety percent (90%) or more of the retail portion of University Village and (b) Crate & Barrel, Apple, Victoria's Secret and Talbots (the "Named Tenants") have signed leases and are scheduled to open no later than sixty (60) days following the date Tenant is required to open for business hereunder. Landlord shall verify the foregoing in writing and provide a leasing plan showing the names, square foot areas and opening dates of the Named Tenants no later than forty-five (45) days prior to the date Tenant is scheduled to commence construction.

3.2 Landlord's and Tenant's Work.

(a) If the Leased Premises are not presently complete, Landlord shall deliver to Tenant, and Tenant agrees to accept from Landlord, possession of the Leased Premises forthwith upon Substantial Completion of Landlord's Work as described in Exhibit C hereto ("Landlord's Work"). Landlord shall, at its sole cost and expense, as soon as it is reasonably possible after the execution of this Lease, commence and pursue to completion the Landlord's Work shown on and/or described in the attached Exhibit C. "Substantial Completion of Landlord's Work" occurs when Landlord, or its project architect, notifies Tenant in writing that the Leased Premises are substantially complete to the extent of Landlord's Work specified in Exhibit C hereof, with

the exception of such work as Landlord cannot complete until Tenant performs necessary portions of its work. Tenant shall commence the installation of fixtures,

equipment and any of its work as set forth in Exhibit C ("Tenant's Work") promptly upon Substantial Completion of Landlord's Work, and Tenant shall diligently pursue such work to completion. There shall be no chargebacks to Tenant for the cost of any item included in Landlord's Work and/or performed prior to delivery of the Leased Premises to Tenant (i.e., so-called "back charges") and Tenant shall not be obligated to pay any additional construction charges or fees such as, without limitation, barricade charges, freight elevator fees, dumpster or other trash fees, sprinkler system shut-down fees or other such charges for work which is not included in Tenant's Work. Prior to installation of a temporary barricade in front of the Leased Premises, Tenant shall provide Landlord with barricade appropriate artwork for an "opening soon" advertisement thereon.

(b) **Punchlist.** Not later than thirty (30) days after Substantial Completion of Landlord's Work, Tenant shall deliver to Landlord a "punchlist" of defects in Landlord's Work. Landlord shall promptly cure such defects at Landlord's sole cost and expense. Latent defects appearing as a result of Landlord's Work shall not be deemed waived until the first anniversary of the Commencement Date. Upon the first anniversary of the Commencement Date, all latent defects shall be waived unless Tenant shall have given notice of the same to Landlord prior to such first anniversary. However, Landlord shall warrant all repairs made in response to any notice of latent defects within the one (1) year period for a period of one (1) year from the date of repair. Notwithstanding such waiver, Landlord's obligations to make repairs set forth explicitly elsewhere in this Lease shall not be subject to the one-year limitation described in this paragraph.

3.3 Statement as to Lease Term. When the Commencement Date has been determined as provided in Section 3.1, Landlord and Tenant shall execute, acknowledge and deliver a written statement specifying the Commencement Date and Expiration Date.

4. RENT.

4.1 Minimum Rent. Tenant shall pay to Landlord, without notice or demand and without any set-off or deduction whatsoever (except as set forth in Section V of Exhibit C attached hereto), the Minimum Rent set forth in Section 1.2 above (the "Minimum Rent"), which shall be paid in advance on or before the first day of each calendar month of the Lease Term. If the Lease Term commences on a day other than the first day of a calendar month or expires on a day other than the last day of a calendar month, the Minimum Rent for such month shall be paid together with the Minimum Rent for the first full month, and shall be a prorated portion of the monthly Minimum Rent, based upon a thirty (30) day month. Notwithstanding anything to the contrary contained herein, provided Tenant is not then in default of this Lease beyond any applicable notice and cure periods, Minimum Rent shall be abated (i) for the one hundred eighty (180) day period following Landlord's delivery of the Leased Premises to Tenant and (ii) during the months of January and February, 2005.

(a) **Future Expansion.** [omitted]

(b) **Renovation or Expansion of Common Areas.** [omitted]

4.2 Landlord's Security. [omitted]

4.3 Percentage Rent.

(a) **Percentage Rent.** In addition to the Minimum Rent to be paid by Tenant pursuant to Section 4.1 above, Tenant shall pay to Landlord Percentage Rent in a sum equal to five percent (5%) of the amount of Tenant's Gross Sales as defined below, during each Lease Year of the Lease Term in excess of the "Breakpoint." Commencing with the first month of the Lease Year when total Gross Sales for the Lease Year exceed the applicable Breakpoint for such Lease Year, Tenant shall pay to Landlord, within twenty (20) days after the end of each calendar month, the Percentage Rent for such calendar month. The Breakpoint during any Lease Year shall be the Minimum Rent payable with respect to such Lease Year divided by .05 (the "Natural Breakpoint"). For example if the Minimum Rent is \$296,000, then the Breakpoint is $\$296,000 / .05 = \$5,920,000$. It is acknowledged by the parties that the Breakpoints applicable to a given full lease year are computed by dividing the Minimum Rent payable by Tenant for that same Lease Year by five percent (5%). All computation and/or reconciliation of Percentage Rent payable by Tenant for a full Lease Year shall be determined in accordance with and governed by the foregoing sentence. Notwithstanding anything to the contrary herein, for the purposes of calculating the Breakpoint only, Minimum Rent shall be deemed paid in full during any portion of the rent abatement period described in Section 4.1 that Tenant is open for business in the Leased Premises.

Percentage Rent for any partial Lease Year shall be established by multiplying the percentage rental due for the twelve month period following the Commencement Date with respect to a partial lease year at the beginning of the term or the 12 month period preceding the expiration date with respect to a partial lease year at the end of the term by a fraction, the numerator of which shall be the number of days in the partial lease year and the denominator of which shall be 365.

(b) **Tenant's Statements Regarding Gross Sales.** Tenant shall provide Landlord with an unaudited monthly statement of Gross Sales within twenty (20) days after the end of each calendar month, certified by Tenant to be correct, which shall show Gross Sales and an itemization of any exclusions or deductions therefrom for such month, as well as year-to-date amounts for the current Lease Year. If any Percentage Rent is due for such month, the payment shall accompany such statement. In addition to such regular monthly statements, Tenant shall provide an annual statement within sixty (60) days after the end of each Lease Year, which shall show the total amount of Gross Sales for such Lease Year, and shall be certified to be true, complete and correct by Tenant, or in Landlord's reasonable discretion following occurrence of an Event of Default as a result of Tenant's failure to comply with Section 4.3, an independent certified public accountant reasonably satisfactory to Landlord. If such annual statement shows that Tenant underpaid Percentage Rent for such Lease Year, Tenant shall include the additional amount, together with interest at the Default Rate with such statement, and if such statement shows that Tenant overpaid Percentage Rent, Landlord shall provide a credit or refund.

(c) **Tenant's Records.** Tenant shall keep full, complete and proper books,

records and accounts prepared in accordance with generally accepted accounting principles (collectively, "Tenant's Records") of its daily Gross Sales in, upon, or from the Leased Premises. Original sales records shall be separately maintained for the Leased Premises and shall include: (i) daily dated sealed, continuous, cash register tapes, (ii) serially numbered sales slips, (iii) settlement report sheets of transactions with subtenants, concessionaires and licensees, (iv) bank statements, (v) general ledger or summary record of all receipts and disbursements from operations in, at or from the Leased Premises, (vi) state and local sales and use tax returns, and (vii) such other records that would normally be kept pursuant to generally accepted accounting principles, or as the Landlord may reasonably require in order to determine Gross Sales hereunder. Tenant shall be permitted to use such cash registers and maintain its business records in the same manner as all of Tenant's other stores. Landlord and its agents and employees shall have the right at any and all reasonable times upon fourteen (14) days prior written notice to Tenant, to examine and inspect all of the books and records of Tenant, including any sales tax reports pertaining exclusively to the business of Tenant conducted in, upon or from the Leased Premises, for the purpose of investigating and verifying the accuracy of any statement of Gross Sales, but in no event more than one (1) time per year. Tenant may excise any portions of such sales tax reports pertaining to other stores owned or operated by Tenant. Tenant shall keep all such records for a period of three (3) years. All records shall be maintained by Tenant on the Leased Premises, or at the corporate office of Tenant.

(d) Audit. Landlord may from time to time (but not more frequently than once each calendar year), upon fourteen (14) days prior written notice to Tenant, cause a complete audit or examination to be made of Tenant's Records and such books and records of any subtenant, licensee or concessionaire for all or any part of the three Lease Years immediately preceding such notice. During such audit, Landlord or its authorized representatives shall have full and free access to Tenant's Records and the right to require that Tenant, its agents and employees furnish such information or explanation with respect to such items as may be necessary for a proper examination and audit thereof. Tenant may, however, excise any portions of tax returns pertaining to other stores owned or operated by Tenant. If such audit or examination discloses that any of Tenant's statements of Gross Sales understates Gross Sales made during any Lease Year by three percent (3%) or more which resulted in underpayment of Percentage Rent, or if Tenant shall have failed to furnish Landlord any monthly Gross Sales statements during any Lease Year or shall have failed to prepare and maintain Tenant's Records as required herein, Tenant shall pay Landlord the reasonable cost of such audit or examination, including reasonable travel and related expenses, and any deficiency in Percentage Rent, with interest at the Default Rate. If such audit or examination shall disclose an understatement of more than ten percent (10%) which results in underpayment of Percentage Rent, upon the second occurrence of such understatement of more than 10% which results in underpayment of Percentage Rent, Landlord shall also have the right to cancel this Lease by written notice given to Tenant within six (6) months after such audit. Landlord's acceptance of Percentage Rent shall be without prejudice to the Landlord's examination, audit and other rights hereunder. Any information obtained by Landlord pursuant to its audit shall be treated as confidential and shall not be disclosed except (i) in connection with litigation with Tenant, (ii) to prospective purchasers or lenders of University Village and (iii) as may be required by law.

(e) Gross Sales Defined. "Gross Sales" shall mean the entire amount of the actual sale price, whether for cash, credit or otherwise, of all sales of goods and services and all other income and receipts whatsoever of all business conducted at, on or from the Leased Premises, including, without limitation:

- (i) mail, telephone, facsimile, E-mail, Internet and other orders originating in, at, from or arising out of the use of the Premises,
- (ii) deposits not refunded to purchasers
- (iii) gross receipts from vending and game machines, except those for exclusive use of employees (inclusion of this definition shall not be construed to authorize vending or game machines)
- (iv) sale price of gift and merchandise certificates
- (v) payments from other parties for shelf or advertising space at or respecting the Leased Premises
- (vi) the full value of all consideration other than money received
- (vii) all other gross income or receipts from any business or operation at, on or from the Leased Premises
- (viii) Gross Sales by any sublessee, concessionaire or licensee.

However, Gross Sales shall not include (but Tenant's Records shall itemize):

- (a) returns to shippers or manufacturers
- (b) any cash or credit refunds made upon any sale in or from the Leased Premises where the merchandise is returned by the customer,
- (c) any sales, use or excise tax imposed by any duly constituted governmental authority (provided that no income or franchise tax, capital stock tax, tax based upon assets or net worth, or similar tax shall be deducted from Gross Sales)
- (d) sales to employees at a discount (not to exceed 2.5% of Gross Sales)
- (e) the exchange of merchandise between the stores and warehouses of Tenant, if any, where such exchange of merchandise is made solely for the convenient operation of the business of Tenant and not for the purpose of consummating a sale that was made in or from the Leased Premises
- (f) postage, parcel post freight, express or other delivery charges paid in connection with any sale
- (g) discounts, allowances and refunds to customers
- (h) layaways until the sale is completed or the deposit abandoned by the customer
- (i) bad debts written off by Tenant for income tax purposes (not to exceed in the aggregate 1% of Gross Sales), provided that if later collected, the amount shall be included in Gross Sales in the year in which collected
- (j) luxury and excise taxes levied upon the purchase of merchandise manufactured by Tenant
- (k) bulk sales of inventory, including damaged or aged merchandise, sales of fixtures and equipment, and sales to jobbers
- (l) charges for repairs, alterations, delivery and gift wrapping of merchandise,

- (m) proceeds of claims for damaged merchandise

- (n) catalog sales of goods not stocked on the Leased Premises, not to exceed three percent (3%) of Gross Sales
- (o) workroom, alteration, shipping and delivery charges, and charges for check cashing and wrapping, at no profit to Tenant

No deduction shall be allowed for any uncollected or uncollectible amounts or reserves therefor, nor for cost of products or services sold, or other costs, charges or expenses of purchasing, financing, selling, transportation, overhead or taxes except as set forth above.

(f) No Partnership. It is understood and agreed that the fixing of a portion of the rental on a percentage of the sales of the business to be done by Tenant does not create a partnership or joint venture relationship between the parties hereto, that Landlord assumes no liability hereunder for the operation of the business of Tenant, and that the provisions with reference to rents herein are for the sole purpose of fixing and determining the total rents to be paid by Tenant to Landlord.

(g) No Waiver. The acceptance by Landlord of any monies paid to Landlord by Tenant pursuant to this Section 4.3 shall not be an admission by Landlord of the accuracy of any monthly or annual statement furnished by Tenant during the month or year reported therein, or of the sufficiency of the amount of any such payment. Landlord shall be entitled to inspect the books and records of Tenant and receive any additional sums due from Tenant disclosed by such inspection, as described above.

(h) No Diversion. To ensure that the Leased Premises will produce an optimum volume of gross sales, Tenant covenants not to divert elsewhere any business, trade or commerce which would ordinarily be transacted by Tenant at, in, on, from or arising out of the Leased Premises.

(i) Opening for Business; Continuous Operations. Because of the difficulty and impossibility of determining Landlord's damages by way of loss of anticipated Percentage Rent from Tenant or from other tenants or occupants of University Village or by way of loss of value of the property, if Tenant, subject to Section 30.12 hereof, shall fail to take possession of the Leased Premises and open for business within thirty (30) days of the time provided herein, or shall abandon the Leased Premises, cease operating or conducting Tenant's business therein, or fail to maintain business hours in accordance with the terms of this Lease following 48 hours notice from Landlord, then Landlord shall have the right, in addition to any or all other rights or remedies under this Lease or at law or in equity, to collect not only Minimum Rent and all other items of Additional Rent herein, but also Additional Rent equal to Two Hundred Fifty Dollars (\$250.00) per day for each day or portion thereof Tenant is required to be open and is not open, subject to Section 30.12 hereof (provided that in the case where Tenant has opened its store to the public, but is late opening on a particular business day, the \$250 Additional Rent shall not apply until the second such late opening following notice by Landlord to Tenant of the first late opening each Lease Year). Such Additional Rent shall be deemed to be liquidated damages in lieu of any Percentage Rent that might have been paid during such period.

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Acceptance by Landlord of such liquidated damages shall not be deemed permission for Tenant to continue such violation, and shall not preclude Landlord from seeking any other remedy for such violation, including, but not limited to, specific performance or termination of this Lease.

4.4 Tenant to Share Expenses. It is intended that this shall be a "net lease" in that tenants in University Village collectively shall pay all operating, repair and maintenance costs and expenses of any kind or nature. In addition to the Minimum Rent, Tenant shall pay to Landlord, as Additional Rent (defined below), in the manner provided in Subsection 4.4(e) below, Tenant's share of all operating, maintenance and repair costs, charges and expenses incurred by Landlord with respect to University Village, except as otherwise specified herein, including, without limitation, the items described in Subsections 4.4(a) through (d) below (herein collectively called "Other Charges"). For purposes of this Section, the term "Accounting Period" shall mean each consecutive twelve (12) month period during the Lease Term commencing July 1 and expiring the following June 30 or, if so determined by Landlord at any time during the Term of this Lease, the calendar year.

(a) Tenant's Share of Taxes. Tenant shall pay to Landlord, as Additional Rent, in the manner provided in Section 4.4(e), Tenant's share of the total amount of real estate taxes ("Taxes") on University Village. For purposes of this Section, the term "Taxes" shall be an amount equal to all real estate taxes and assessments (including but not limited to local improvement district, road improvement district and water improvement district assessments provided such assessments do not relate to the initial development of University Village), if any, that are levied upon or assessed against University Village during the Lease Term. Tenant's share of Taxes shall be an amount equal to the total Taxes due and payable during each calendar year of the Lease Term with respect to the lands and improvements comprising University Village, deducting any contribution toward Taxes and Insurance by other parties who are not paying a proportionate share of same, multiplied by Tenant's Fraction; provided, however, that if any tenants in any building or buildings pay real estate taxes directly to any taxing authority as may be provided in their leases, their square footage shall not be deemed a part of the denominator used for purposes of computing Tenant's share of Taxes. Tenant shall not be required to reimburse Landlord for taxes based upon the following: (1) rent taxes (except to the extent that same are directly assessed against the tenants by the taxing authority), (2) gross receipts taxes levied on gross receipts of landlord, (3) income taxes, (4) franchise taxes, (5) transfer taxes, (6) inheritance taxes, and (7) capital stock taxes. Tenant shall not be obligated to reimburse Landlord for any penalty or interest for the late payment by Landlord of taxes. Landlord shall promptly pay or credit to Tenant, Tenant's proportionate share of any refunds or rebate of Taxes after deducting reasonable expenses incurred by Landlord in obtaining same.

(b) Tenant's Share of Insurance. Tenant shall pay to Landlord, as Additional Rent, in the manner provided in Section 4.4(e), Tenant's share of the cost of insurance for University Village. The cost of insurance ("Insurance") shall include all insurance premiums for fire, all risk endorsement coverage, earthquake, liability, loss of rental income, and any other insurance that Landlord deems necessary or desirable to cover University Village. Tenant's share of Insurance shall be an amount equal to the total of such premiums paid during each Accounting Period or portion thereof of the Lease Term, after deducting any contribution toward Taxes and

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Insurance by other parties who are not paying a proportionate share of same, multiplied by Tenant's Fraction.

(c) University Village Expenses. Tenant shall pay to Landlord, as Additional Rent, in the manner provided in Section 4.4(e), Tenant's share of the operating costs ("University Village Expenses") of University Village, including all common areas and facilities (collectively, the "Common Area"). Tenant's share of University Village Expenses shall be an amount equal to the total University Village Expenses during each actual Accounting Period, or portion thereof, during the Lease Term multiplied by Tenant's Fraction.

“University Village Expenses” shall mean, without duplication, all expenses, costs and amounts of every kind and nature (to the extent not a capital expense) which Landlord shall pay during any calendar year any portion of which occurs during the Term in connection with the management, repair, maintenance, replacement, insurance and operation of University Village, including, without limitation, any amounts paid for:

- (a) utilities serving the common areas, including but not limited to electricity, power, gas, steam, oil or other fuel, water, sewer, lighting, heating, air conditioning and ventilating
- (b) permits, licenses and certificates necessary to operate and manage University Village, and costs of complying with other legal requirements, including, without limitation, the Americans with Disabilities Act, 42 U.S.C. 12101 et seq. and the regulations promulgated thereunder
- (c) supplies, materials, tools, equipment, and vehicles used in the operation, repair, maintenance and security, floor care and cleaning, landscaping, and other services for University Village, including rental, installment purchase and financing agreements therefor and interest thereunder
- (d) reasonable accounting, legal, inspection, consulting and other services for services performed for University Village
- (e) wages, salaries, bonuses, and other compensation and benefits for any on-site manager, personnel and other parties engaged in the operation, maintenance or security of University Village, and employer’s Social Security taxes, unemployment taxes or insurance, and any other taxes which may be levied on such wages, salaries, compensation and benefits, data or payroll processing expenses relating thereto (if the manager or other personnel are located off-site and handle other properties, the foregoing expenses shall be allocated appropriately between University Village and such other properties)
- (f) payments under any easement, operating agreement, declaration, restrictive covenant, or instrument pertaining to the sharing of costs in any development of which University Village is part
- (g) alarm monitoring and security service, janitorial service, trash removal, removal of ice and snow (and salting and sanding in connection therewith)
- (h) parking surcharges or fees that may result from any environmental or other law or guideline, and the cost of obtaining, providing and operating public transportation or shuttle bus systems to bring customers or workers to or from University Village if

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- (i) required by such laws or guidelines, or if otherwise deemed desirable by Landlord
- (j) the costs of operating and maintaining any on-site office at University Village, including without limitation, the fair rental value thereof, telephone charges, postage, stationery and photocopying expenses
- (k) music programs and equipment, whether rented or purchased
- (l) telephone directory listings for University Village
- (m) appropriate reasonable reserves for operation of University Village and for covering uninsured portions, including deductible amounts, of casualty damage and general liability claims relating to the University Village
- (n) operation, maintenance, repair, installation and replacement (to the extent not a capital expense), inspection, testing, painting, decorating and cleaning of: (i) elevators, escalators, fire exits, pedestrian bridges, skywalks, skybridges, arrival zones and stairways, (ii) sidewalks, curbs, gutters, guardrails, bumpers, fences, flagpoles, flags, banners, bicycle racks, University Village identification and pylon signs, directional signs, hand-out pamphlet directories, traffic signals and markers, including those located off-site but installed for the benefit of University Village, (iii) parking structures, parking lots, loading and service areas and driveways (including sweeping, cleaning, re-striping, repairing, sealing, re-surfacing and replacement), (iv) storm and sanitary drainage systems, including disposal plants, lift stations and detention ponds and basins, (v) irrigation systems, (vi) any Systems and Equipment, (which shall mean any plant, machinery, transformers, ducts, cables, wires, and other equipment, facilities, and systems designed to supply light, heat, ventilation, air conditioning and humidity or any other services or utilities, or comprising or serving as any component or portion of any electrical, gas, steam, plumbing, water, sewer, sprinkler, communications, alarm, security, or fire/life/safety systems or equipment, or any other mechanical, electrical, electronic, computer or other systems or equipment for University Village and depreciation relating thereto, (except to the extent that any of the same serves any tenant exclusively or is subject to shared tenant use), (vii) exterior planting, replanting and replacement of flowers, shrubbery, plants, trees, grass, sod, plants in hanging baskets, and other landscaping, (viii) all portions of buildings, both interior and exterior, in the University Village, including without limitation, Common Areas and fixtures, equipment and other items therein or thereon, including but not limited to floors, floor coverings, corridors, ceilings, foundations, walls, wall-coverings, restrooms, lobbies, canopies, skylights, trash and ash cans and receptacles, trash compactors, planters, waterfalls, fountains, pools, benches, furniture, doors, locks and hardware, windows, glass and glazing, (ix) gutters and downspouts, roof flashings and roofs (including repairs and replacements)
- (n) an amount equal to fifteen percent (15%) of all of the foregoing costs and expenses (excluding insurance premiums, utilities and taxes) as a liquidation of Landlord’s general overhead (which amount shall be in addition to the compensation and related expenses for the manager and other aforementioned expenses). The foregoing provision is for definitional purposes only and shall not be construed to impose any obligation upon Landlord to incur such expenses.

The following items are to be excluded from such operating expenses:

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- A) Costs attributable to seeking and obtaining new tenants as well as retaining existing tenants - such as advertising, brokerage commissions, architectural, engineering, attorney’s fees, renovations and improvements;
- B) Costs that are reimbursed to the Landlord by tenants as a result of provisions contained in their specific leases;
- C) Costs for alterations and additions that are in the nature of capital improvements;
- D) Costs for capital improvements and repairs;
- E) Costs incurred due to violations by the Landlord of any of the terms and conditions of any leases in the center;

- F) Interest on any mortgages of the Landlord and rental under any ground or underlying lease;
- G) Rentals and other related expenses incurred in leasing air conditioning systems, elevators or other equipment ordinarily considered to be of a capital nature, except equipment used in providing janitorial services not affixed to the building;
- H) All items and services for which other tenants have reimbursed Landlord or have paid third persons directly;
- I) Advertising and promotional expenditures in excess of those amounts provided in Section 27 below, unless part of a specific marketing plan agreed upon by the tenants;
- J) Repairs and other work occasioned by fire, windstorm or other casualty to the extent that the Landlord is reimbursed by insurance that was required to be carried under the lease;
- K) Costs incurred in operating and maintaining the project's parking facilities if the Landlord charges for parking, unless Landlord uses the income from the parking facility as a credit against operating expenses;
- L) Any costs, fines or penalties incurred due to violations by Landlord of any governmental rule or authority;
- M) Costs for sculpture, paintings or other objects of art to the extent such are items of a capital nature;

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- N) Costs attributable to repairing items that are covered by warranties to the extent such costs are reimbursed pursuant to such warranties; and
- O) Repairs and maintenance performed in a tenant's exclusive space and not in the common areas.

Provided the Term of the Lease commences in the 2004 calendar year, Tenant's share of the following Other Charges shall not exceed the caps set forth herein for the first twelve (12) months of the Term. In the event that the Term commences in a calendar year subsequent to the 2004 calendar year, then the following caps shall be increased by five percent (5%) for each calendar year thereafter until the Term commences. All Other Charges stated on a per square foot basis shall be calculated on the ground level portion of the Area of Leased Premises only.

University Village Expenses:	\$6.20 per square foot
Insurance:	\$0.97 per square foot
Taxes:	\$3.53 per square foot

(d) Heating and Air Conditioning Charge. Tenant shall contract for service and maintenance checks and filter changes for the heating and air conditioning system serving the Leased Premises, and Tenant shall pay the cost thereof. Tenant shall provide to Landlord, upon Landlord's reasonable request for the same, copies of all work orders and other documents necessary to verify that the heating and air conditioning system serving the Leased Premises has been and is being adequately serviced, maintained and inspected on a regular basis, which need not exceed once every calendar quarter. If Tenant shall fail to contract for such service and maintenance to be performed, Landlord, following reasonable notice to Tenant, may elect to perform such service and maintenance and Tenant shall pay to Landlord the costs thereof immediately upon receipt of billing therefor. Such payments shall be deemed Additional Rent hereunder.

(e) Payment of Other Charges. Within sixty (60) days after the expiration of each Accounting Period of the Lease Term (or as soon thereafter as such information becomes available), Landlord will notify Tenant in writing of Landlord's estimate of Tenant's share of the Other Charges due for the then current Accounting Period. Landlord's estimate shall be based upon the actual amount of the Other Charges for the previous Accounting Period plus Landlord's reasonable estimate of the increase in such operation costs for the then current Accounting Period. Notwithstanding Landlord's actual estimate, in no event shall Tenant's payment to Landlord for the portion of University Village Expenses payable by Tenant increase by more than five percent (5%) per year on a non-cumulative basis. Tenant shall pay the estimated Tenant's share in advance in equal monthly installments on the first day of each month of such Accounting Period. Within sixty (60) days after the end of each Accounting Period, Landlord will compute Tenant's share for such Accounting Period based upon the actual amount of the Other Charges for that Accounting Period. Landlord shall furnish Tenant with a reasonably detailed statement of Tenant's proportionate share, and if the total amount paid by Tenant for such Accounting Period is less than the actual amount of Tenant's share for such Accounting Period, Tenant shall pay Landlord any deficiency, subject to the 5% cap on annual increases described above. If the

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total amount paid by Tenant for such Accounting Period exceeds the actual amount of Tenant's share, Landlord shall credit such excess to the next monthly payments of Tenant's share which thereafter come due. Any excess payments made by Tenant of taxes, common area maintenance expenses, promotional fund payments, Merchants' Association Dues or any other items of Additional Rent, shall be refunded to Tenant within thirty (30) days following reconciliation of the accounting period for which such payments were made, unless credited to the next Rent due. If this Lease expires at a time other than the expiration date of an Accounting Period, Tenant shall be obligated to pay immediately any deficiencies which shall be computed at the expiration of that Accounting Period. If the estimated amount Tenant has paid for that Accounting Period exceeds the actual amount of Tenant's share, and if Tenant has otherwise complied with all of the terms and provisions of this Lease, Landlord shall refund such excess to Tenant. If at any time during an Accounting Period after the first Lease Year, the amount of the Other Charges increases over the actual amount thereof for the preceding Accounting Period, Landlord may, at its election, but not more than once in any Accounting Period and subject to the cap on increases, adjust the amount of monthly estimated installments due during the balance of that calendar year to reflect such increase. Any increased payments required to be made pursuant to this Section shall be made within thirty (30) days after Landlord has notified Tenant thereof. Tenant's obligations under this Section shall survive the expiration or termination of this Lease. Landlord shall provide Tenant with a receipted copy of the tax bill upon Tenant's written request.

(f) Disputes. Within two (2) years after receipt by Tenant of any statement from Landlord with respect to payment of charges pursuant to this Section 4.4, if Tenant disagrees with such statement for any reason, Tenant shall notify Landlord in writing stating the basis of such objection. Failure to object in writing during such two year period shall be deemed Tenant's agreement with such statement and Tenant waives the right to dispute any such statement after the expiration of such two year period. In the event of any dispute regarding the applicability, amount, or other matter

relating to Other Charges hereunder, such dispute shall be resolved on the basis of an investigation, analysis and report prepared by Landlord's independent certified public accounting firm, which report shall be conclusive and binding upon the parties.

5. USE OF PREMISES AND OPERATION OF TENANT'S BUSINESS.

5.1 Permitted Uses. Tenant shall not use or permit or suffer the use of the Leased Premises for any business or purpose or under any other trade name other than the Permitted Uses set forth at Section 1.11 above and Tenant's Trade Name set forth in Section 1.12 above or under such other name as is used by Tenant for a majority of its stores, including all of its stores in the Pacific Northwest (defined as Northern California, Oregon and Washington), without the prior written consent of Landlord. Tenant expressly understands and acknowledges that its Permitted Use is nonexclusive and that other tenants or occupants within University Village may sell items similar to those sold by Tenant. Permitted Use is a material consideration to Landlord in order to maintain an appropriate tenant mix in University Village and achieve maximum gross sales for all tenants and to insure continual operation of a full-service shopping center. Landlord shall have no obligation to consent to any change in the Permitted Uses for the Leased Premises.

5.2 Permitted Trade Name. Landlord does not represent that Tenant may use the

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Tenant's permitted trade name and Tenant shall indemnify Landlord against any claims, suits, costs, liabilities and expenses, including attorneys' fees, arising from use of Tenant's permitted trade name by Tenant, including any infringement claims. Tenant warrants that it has the full and unfettered right to use Tenant's trade name for the entire term of this Lease and such use will not in any way infringe on the rights of others.

5.3 Uses Prohibited. Tenant shall not do or permit anything to be done in or about the Leased Premises nor bring or keep anything therein which will in any way increase the existing rate of, or affect, any fire or other insurance upon the Leased Premises or the building of which the Leased Premises are a part, or cause a cancellation of any insurance policy covering the Leased Premises or building or any part thereof or any of its contents. Tenant shall not do or permit or suffer anything to be done in or about the Leased Premises which will in any way obstruct or interfere with the rights of other tenants or occupants of University Village or injure or harass them, nor shall the Tenant use or allow the Leased Premises to be used for any purpose which is objectionable or offensive in Landlord's reasonable judgment or is unlawful. If Tenant permits or engages in any activity which, in Landlord's reasonable judgment, is objectionable, offensive or otherwise constitutes a nuisance to the customers or other tenants of University Village, Tenant shall, within thirty (30) days after written notice from Landlord, discontinue such practice. Tenant's failure to comply shall constitute a default under this Lease and entitle Landlord to pursue its remedies for default or, in the alternative, perform such work required on behalf of Tenant and recover, as Additional Rent, the cost thereof, plus interest thereon at the Default Rate on the first day of each month, commencing on the date due through the date of payment. Such Additional Rent shall become due and payable to Landlord twenty (20) days following completion of the work and delivery of an invoice for same to Tenant. Tenant shall not use, occupy, suffer or permit any portion of the Leased Premises to be used as an office (other than incidental office use in connection with the Permitted Uses), living, sleeping or lodging quarters. Tenant shall not display any merchandise or sign outside the Leased Premises or in any way obstruct the malls or sidewalks adjacent thereto or otherwise solicit business within the Common Areas except as specifically allowed in writing by Landlord. Landlord reserves and retains the right not to approve or consent to any proposed exterior display of goods or signs. Tenant shall not, without the prior written consent of Landlord, use the name of University Village for any purpose other than the address of the Leased Premises. In any event, Tenant shall not acquire any rights in or to such name.

5.4 Operation of Business. Tenant shall conduct its business on the Leased Premises during the entire Lease Term hereof with diligence and efficiency, consistent with prudent business practices, so as to produce the optimum amount of gross sales which may be produced by such business, unless prevented from doing so by causes beyond Tenant's control. Tenant shall keep the store shelves on the Leased Premises fully and continuously stocked with all standard merchandise and products for the purpose of operating its business and shall maintain an adequate sales force. Subject to the provisions of this Lease, Tenant shall continuously during the entire Lease Term hereof conduct and carry on Tenant's business in the Leased Premises and shall keep the Leased Premises open for business during at least the days, nights and hours designated from time to time by Landlord as the hours of operation for University Village (which are currently Monday through Saturday 10:00 a.m. to 8:00 p.m. and Sunday 11:00 a.m. to 6:00 p.m.),

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provided at least ninety percent (90%) of all other retail tenants are open such hours; provided, however, that this provision shall not apply if the Leased Premises should be closed and the business of Tenant temporarily discontinued thereon on account of strikes, lockouts or similar causes beyond the reasonable control of Tenant. Notwithstanding anything to the contrary herein or any amendments hereto, nothing in this Lease shall be construed, interpreted or deemed to authorize the cessation of Tenant's operations in the Leased Premises nor to authorize Tenant to "Go Dark" at any time during the Lease Term, as it may be extended. Tenant's failure to open for business or to maintain business hours in accordance with this Section 5.4 shall be subject to payment of Additional Rent as provided in Section 4.3(i) above, without limitation of any other remedies available to Landlord with respect to such default under this Lease, at law or otherwise. Tenant shall not be required to participate in any "midnight madness" or "sidewalk sales" or any similar type of sale that Tenant reasonably deems inappropriate with its corporate image. Notwithstanding any other requirements set forth in this Lease, Tenant shall have the right to close its store for business on the following days: New Year's Day, Thanksgiving Day and Christmas Day and one (1) other day each year for the taking of inventory and up to ten (10) days during the Term for repairs and renovations; provided that Tenant shall give Landlord at least 10 days prior written notice of such closures for repairs.

5.5 Compliance with Laws. Tenant shall not use the Leased Premises in any way (or permit or suffer anything to be done in or about the Leased Premises) which will conflict with any law, statute, ordinance or governmental rule or regulation or any covenant, condition or restriction (whether or not of public record) affecting University Village, now in force or which may hereafter be enacted or promulgated. Tenant shall, at its sole cost and expense, promptly comply with (a) all laws, statutes, ordinances, and governmental rules and regulations, now in force or which may hereafter be in force, including, without limitation, the Americans with Disabilities Act, 42 U.S.C. 12101 et seq. and the regulations promulgated thereunder, (b) all requirements, covenants, conditions and restrictions, now in force or which may hereafter be in force, and (c) all requirements (now in force or which may hereafter be in force) of any board of fire underwriters or other similar body now or hereafter constituted relating to or affecting the condition, use or occupancy of the Leased Premises. The judgment of any court of competent jurisdiction or the admission by Tenant in any action against Tenant, whether Landlord be a party thereto or not, that Tenant has violated any law, statute, ordinance, governmental rule or regulation or any requirement, covenant, condition or restriction shall be conclusive of the fact as between Landlord and Tenant. Landlord shall comply with legal requirements applicable to the Leased Premises, including without limitation, the

Americans with Disabilities Act, 42 U.S.C. 12101 et seq. and the regulations promulgated thereunder, insofar as they require structural repairs, improvements or alterations to the roof, foundation, columns, load-bearing walls, lintels, beams or any exterior portion of the Leased Premises.

5.6 Deliveries. Tenant shall load and unload merchandise, supplies, fixtures, equipment and furniture, and cause the collection of rubbish, only through rear service door or doors of the Leased Premises. Notwithstanding the foregoing, deliveries by UPS and overnight courier may be made through the front of the Leased Premises. Tenant shall not permit trailers or trucks servicing the Leased Premises to remain parked in University Village beyond periods necessary to service Tenant's operations.

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5.7 Other Stores. Tenant shall not during the first five (5) years following Tenant's opening for business at the Leased Premises, open a "J. Crew" store at the Northgate Mall in Seattle, Washington.

5.8 Co-Tenancy. If at any time during the Lease Term less than eighty-five percent (85%) of the retail portion of University Village is leased and open for business for a continuous period of more than one hundred eighty (180) days, Tenant shall have the option to pay the lesser of (i) Minimum Rent, Percentage Rent and Other Charges, or (ii) ten percent (10%) of Gross Sales in substitution for Minimum Rent, Percentage Rent and Other Charges until such time as Landlord notifies Tenant that at least eighty-five percent (85%) of the retail portion of University Village is leased and open for business. Landlord shall, upon written request of Tenant, verify in writing the names and square foot areas of all tenants open and operating in University Village.

6. UTILITIES.

6.1 Tenant's Obligation. Tenant shall pay before delinquency, at its sole cost and expense, all charges for water, gas, heat, electricity, power, garbage removal, telephone service, and sewer service charges, charged or attributable to the Leased Premises, and all other services or utilities used in, upon or about the Leased Premises during the Lease Term and the cost of installing meters therefor; provided, however, that if any such services or utilities shall be billed to Landlord and are not separately metered to the Leased Premises, the amount thereof shall be prorated, and Tenant shall pay to Landlord upon demand, as Additional Rent hereunder, an amount equal to that proportion of the total charges therefor which the amount of utility services consumed on the Leased Premises bears to the total amount of utility services consumed in the area covered by such combined charges. In no event shall Landlord be liable for services consumed in the area covered by such combined charges. In no event shall Landlord be liable for an interruption or failure in the supply of any such utilities to the Leased Premises unless and to the extent caused by the negligence or willful misconduct of Landlord, its employees, agents or contractors. Tenant shall not overburden or exceed the capacity of any of the utilities serving the Leased Premises. Any interruption or failure of utilities will not constitute a termination or constructive eviction of Tenant. No garbage shall be placed outside of the Leased Premises at any time except in proper, approved containers in designated garbage collection areas. Tenant shall store all trash and refuse in appropriate containers within the Leased Premises and attend to the daily disposal thereof in the manner designated by Landlord. If Landlord supplies utilities to Tenant, Tenant shall purchase such utilities from Landlord, at Landlord's request, at rates not exceeding the amount Tenant would otherwise be required to pay to the applicable utility company. In the event that Landlord no longer desires to supply any utility service, Landlord agrees to continue to provide such service until suitable arrangements have been made for a public utility to assume the obligation.

6.2 Interruption. Landlord may, with reasonable notice to Tenant, or without notice in the case of an emergency, discontinue gas, water, electricity and any and all other utilities whenever such discontinuance is necessary to make repairs or alterations to the Leased Premises or University Village or for the protection of persons or property. No such action by Landlord

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shall be construed as an eviction or a disturbance of the possession of the Tenant or an election by Landlord to terminate this Lease nor shall Landlord be in any way liable therefor. Notwithstanding the foregoing, in the event Landlord discontinues utility service or such utility service is interrupted by the negligence or willful misconduct of Landlord, its employees, agents or contractors, in excess of 48 hours, Minimum Rent shall abate until service is restored.

7. TENANT TO PAY PERSONAL PROPERTY TAXES. Tenant shall pay, or cause to be paid, before delinquency, any and all taxes levied or assessed during the Lease Term upon all Tenant's leasehold improvements, equipment, furniture, fixtures, and any other personal property located in the Leased Premises. In the event any or all of the Tenant's leasehold improvements, equipment, furniture, fixtures, and other personal property shall be assessed and taxed with the real property, Tenant shall pay to Landlord its share of such taxes within twenty (20) days after delivery to Tenant by Landlord of a statement in writing setting forth the amount of such taxes applicable to Tenant's property. There shall be no duplication of taxes between Sections 4.4 and 7 hereof.

8. LICENSES AND TAXES.

8.1 Tenant's Obligation. Subject to Section 4.4(a), Tenant shall be liable for, and shall pay throughout the Lease Term, all license and excise fees and occupation taxes covering the business conducted on the Leased Premises. Subject to Section 4.4(a), if any governmental authority or unit under any present or future law effective at any time during the Lease Term hereof shall in any manner levy a tax on rents payable under this Lease or rents accruing from use of the Leased Premises or a tax in any form against Landlord because of or measured by revenue derived by Landlord from the leasing or rental of such property or any amounts payable by Tenant hereunder (such as an excise, sales or rental tax), such tax shall be paid by Tenant, either directly or through Landlord, and upon Tenant's default therein, Landlord shall have the same remedies as for failure to pay rent. It is understood and agreed, however, that Tenant shall not be liable to pay any net income tax imposed on Landlord.

8.2 Additional Rent. As used herein, "Additional Rent" shall refer to any amounts payable by Tenant to Landlord under this Lease other than Minimum Rent and Percentage Rent. Additional Rent shall include any such sums whether or not designated as Rent or Additional Rent hereunder. Landlord shall have, with respect to any failure to pay Additional Rent hereunder, all of the remedies as for the failure to pay Minimum or Percentage Rent.

9. ALTERATIONS.

9.1 Acceptance of Leased Premises. Upon completion of Landlord's Work, and except as otherwise provided in Section 3.2(b) hereof, Tenant shall accept the Leased Premises in their then condition "AS IS" and waives the right to make any claim against Landlord for any matter directly or indirectly

arising out of the condition of the Leased Premises, appurtenances thereto, the improvements thereon and the equipment thereof, and Tenant shall thereafter save and hold Landlord harmless from liability as provided in Section 14 of this Lease. Except as set forth in Section 3.2(b), Landlord shall not be liable for any latent or patent defects within the

Leased Premises. Tenant acknowledges neither Landlord nor any agent or employee of Landlord has made any representation with respect to the suitability of the Leased Premises or University Village to the conduct of Tenant's business, nor has Landlord agreed to undertake any modifications, alterations or improvements of the Leased Premises except as expressly and specifically provided in Exhibit C to this Lease.

9.2 Alterations by Tenant.

(a) Consent. Tenant shall not attach any fixtures, equipment or other items to the Leased Premises, or make any alterations, additions or improvements in or to the Leased Premises without the prior written consent of Landlord, which consent may be subject to such conditions as Landlord may reasonably deem appropriate. Notwithstanding the foregoing, Tenant shall have the right to make interior, non-structural design changes to the Leased Premises without Landlord's consent so long as such changes do not affect the mechanical or electrical systems outside of the Leased Premises and in the aggregate cost less than \$50,000. Subject to Section 5.5. Tenant shall make any alterations in or to the Leased Premises which are required to cause the Leased Premises to comply with applicable governmental laws, rules, ordinances or regulations. Any alterations, additions or improvements consented to by Landlord shall be made at Tenant's sole cost and expense. Tenant shall secure any and all governmental permits, approvals or authorizations required in connection with any such work, and shall hold Landlord harmless from any liability, costs, damages, expenses (including reasonable attorneys' fees) and any liens resulting therefrom. Except as otherwise provided herein, upon expiration or sooner termination of this Lease, all alterations, additions and improvements (and expressly including all light fixtures and floor coverings), shall become the property of the Landlord, except trade fixtures, appliances and equipment which do not become a part of the Leased Premises.

(b) Removal upon Termination. Upon the expiration or sooner termination of the term hereof, Tenant shall, at Tenant's sole cost and expense remove its movable trade fixtures, appliances and equipment, and Tenant shall at its sole cost and expense, repair any damage to the Leased Premises caused by such removal.

(c) Plans. No alterations, additions or improvements in or to the Leased Premises shall be done until all of Tenant's plans and specifications have been submitted to and approved by Landlord in writing, all required permits therefor have been obtained from appropriate governmental authorities.

(d) Work. All Work shall be performed: (i) in a thoroughly first class, professional and workmanlike manner, (ii) only with materials that are new, high quality, and free of material defects, (iii) strictly in accordance with plans and specifications approved by Landlord in advance in writing, (iv) not to adversely affect any systems and equipment or structure within University Village, (v) diligently to completion and so as to cause the least possible interference with other tenants and the operation of University Village, and (vi) in compliance with all laws and other provisions of this Lease. Upon completion, the Landlord shall be provided complete "as-built" drawings and specifications for all alterations and additions

to the Leased Premises made by Tenant.

(e) Failure to Prosecute. In the event Tenant is required or undertakes to perform or complete any construction work, installation of fixtures or other construction pursuant to this Lease, either before or after the Commencement Date, if Tenant shall neglect, fail or refuse to commence its work as required or thereafter to diligently proceed and complete such work, then Landlord, in addition to any other rights or remedies it may have, may (i) after thirty (30) days prior written notice to Tenant, complete Tenant's Work at Tenant's expense; (ii) commence or recommence all of Tenant's payment obligations pursuant to this Lease, notwithstanding incompleteness of such work; and/or (iii) proceed pursuant to Section 16 with respect to any default under this Lease.

(f) Completion. Within ninety (90) days after the date upon which Tenant opens for business in the Leased Premises, or following completion of any material alterations, additions or improvements to the Leased Premises, Tenant shall deliver to Landlord the following material: (i) Tenant's certificate stating that the work to be performed by Landlord and Tenant pursuant to the terms of this Lease has been completed in compliance with approved plans and specifications; that no security interest or other lien or claim is outstanding or has been filed with respect to the Leased Premises or the Tenant's interest therein; which certificate may be relied upon by Landlord and any lender or purchaser of University Village; (ii) a certificate of the general contractor performing Tenant's work stating that all subcontractors, laborers and materialmen who have performed work or furnished materials to the Leased Premises have been paid in full and that all liens or rights or claims of lien have been discharged of record or waived; (iii) complete releases and waivers of lien from Tenant's general contractor and from all subcontractors with contracts of \$5,000 or more in recordable form and otherwise in compliance with all applicable Washington law; (iv) Tenant's written acceptance of the Leased Premises; (v) a certificate of occupancy for the Leased Premises issued by the City of Seattle; and (vi) Tenant shall provide a statement as to the dollar value of leasehold improvements (as opposed to equipment and trade fixtures) made by Tenant at Tenant's sole cost and expense to the Leased Premises.

10. MAINTENANCE AND REMODEL OF LEASED PREMISES.

10.1 Maintenance and Repair by Tenant. Tenant shall at all times throughout the Lease Term at its sole cost and expense keep the non-structural portions of the Leased Premises (including exterior doors and entrances, all windows and moldings and trim of all doors and windows) and all partitions, door surfaces, fixtures, equipment and appurtenances thereof (including lighting, heating and air conditioning systems which exclusively serve the Leased Premises) in good order, condition and repair, damage by unavoidable casualty excepted (but not excluding damage from burglary or attempted burglary of the Leased Premises). Without limiting the generality thereof, Tenant shall keep the glass of all windows, doors, and showcases clean and presentable and free of graffiti; replace immediately all broken glass in the Leased Premises; at reasonable intervals as may be required to keep the Leased Premises in a first class condition, paint or refinish the interior of the Leased Premises and the store front, including entrances; make any necessary repairs to, or replacements of, all door closure apparatuses and

mechanisms; keep all plumbing within and exclusively serving the Leased Premises, or where Tenant has caused blockage or some other problem outside the Leased Premises (in which case Landlord may repair such blockage or problem and charge Tenant for the same as provided herein,) clean and in good state of repair including pipes, drains, toilets and basins at Landlord's request, assist Landlord to remove all snow and ice from the sidewalk in front of the Leased Premises; and keep all utilities within and exclusively serving the Leased Premises, or where Tenant has caused blockage or some other problem outside the Leased Premises (in which case Landlord may repair such blockage or problem and charge Tenant for the same as provided herein), in a good state of repair. Tenant shall maintain the Leased Premises free of insects, rodents, and other pests and shall employ a pest exterminating contractor to service the Leased Premises at such intervals as Landlord may reasonably require. Tenant shall maintain the heating, ventilating and air conditioning ("HVAC") equipment and plumbing and electrical installations within and exclusively serving the Leased Premises or where Tenant has caused blockage or some other problem outside the Leased Premises in accordance with such reasonable standards for regular maintenance and repair thereof as Landlord may provide to Tenant from time to time. Tenant shall contract for in its own name and shall pay for a qualified service contractor to inspect, adjust, clean and repair HVAC equipment, including changing filters on a quarterly basis. If Tenant's use of the Leased Premises requires a grease trap, Tenant shall contract for in its own name and shall pay for a qualified service contractor to inspect, clean and repair such grease trap at such intervals as may be required by Tenant's use, but not less frequently than monthly. In the event such grease trap services Tenant and other tenants in University Village, Landlord may elect to perform such inspection, cleaning and repairing and Tenant shall pay to Landlord its proportionate share of the costs thereof immediately upon receipt of billing therefor based on the number of tenants serviced by such grease trap. Such payments shall be deemed Additional Rent hereunder.

10.2 Failure to Maintain. If Tenant fails to keep and preserve the Leased Premises as set forth in Section 10.1 above, Landlord may at its option (following ten (10) business days' notice except in case of emergency) cause the same to be repaired, and in such case, upon receipt of written statements from Landlord, Tenant shall promptly pay the entire cost thereof as Additional Rent. Landlord shall have the right, without liability, to enter the Leased Premises for the purpose of making such repairs upon the failure of Tenant to commence repairs following ten (10) business days notice (except in case of emergency, where Landlord may, but shall not be obligated to, make such repairs immediately).

10.3 Repairs by Landlord. Landlord shall keep the floor slab, columns, the roof, exterior and load bearing walls (other than Tenant's storefront), common utility lines to the point of connection for Tenant, all conduits passing through the Leased Premises servicing exclusively others, foundations and building structure of the Leased Premises in a good state of repair, and shall accomplish such repairs as may be needed reasonably promptly after receipt of written notice from Tenant. Subject to the mutual waiver of subrogation, should such repairs be required by reason of Tenant's negligent acts or failure to act, Tenant shall promptly pay Landlord for the cost thereof as Additional Rent. Except as otherwise specifically provided herein, there shall be no abatement of rent and no liability of Landlord by reason of any injury to or interference with Tenant's business arising from the making of any repairs, alterations or improvements in or to

any portion of the Leased Premises, the building of which the Leased Premises is a part, or in or to fixtures, appurtenances and equipment therein.

10.4 Tenant's Obligation to Remodel the Leased Premises. [omitted]

10.5 Surrender of Leased Premises. At the expiration or sooner termination of this Lease, Tenant shall return the Leased Premises, broom clean, to Landlord in the same condition as received (or, if altered by Landlord or by Tenant with the Landlord's consent, or where consent is not required, in such altered condition), reasonable wear and tear, or damage by casualty leading to termination of this Lease excepted. Tenant shall remove all trade fixtures, appliances and equipment which do not become a part of the Leased Premises, and shall restore the Leased Premises to the condition they were in prior to the installation of such items. Tenant's obligation to perform this covenant shall survive the expiration or termination of this Lease. If Tenant fails to remove any of its property required to be removed hereunder, Landlord may remove and store the same at the expense of Tenant. Any of such property may be sold to cover the expenses of removal and storage if not paid for by Tenant.

11. LIENS AND ENCUMBRANCES.

11.1 Liens. Tenant shall keep the Leased Premises and University Village free from any liens or encumbrances arising out of any work performed, materials furnished or obligations incurred by Tenant, and shall indemnify and hold Landlord harmless from any and all costs, liability or expenses (including reasonable attorneys' fees) arising therefrom. Tenant shall place such contractual provisions as Landlord may reasonably request in all contracts and subcontracts for Tenant's improvements assuring Landlord that no mechanics liens will be asserted against Landlord's interest in the Leased Premises or University Village. Said contracts and subcontracts shall provide, among other things, the following: That notwithstanding anything in said contracts or subcontracts to the contrary, Tenant's contractors, subcontractors, suppliers and materialmen (hereinafter collectively referred to as "Contractors") will perform the work and furnish the required materials on the sole credit of Tenant; that no lien for labor or materials will be filed or claimed by the Contractors against Landlord's interest in the Leased Premises or University Village; that the Contractors will immediately discharge any such lien filed by any of the Contractor's suppliers, laborers, materialmen or subcontractors; and that the Contractors will indemnify and save Landlord harmless from any and all costs and expenses, including reasonable attorneys' fees, suffered or incurred as a result of any such lien against Landlord's interest that may be filed or claimed in connection with or arising out of work undertaken by the Contractors.

11.2 Claims. If any lien is filed against the Leased Premises or University Village by any person claiming through Tenant, Tenant shall discharge the same by payment or by providing a bond in form and amount and issued by a surety reasonably satisfactory to Landlord adequate to discharge the same as a lien against the Leased Premises and University Village. If Tenant shall fail to cause such lien to be discharged of record, within thirty (30) days following written notice from Landlord, Landlord may pay or otherwise discharge the same by paying the amount claimed to be due and the amount so paid by Landlord, including reasonable attorneys' fees incurred by Landlord in defending against such lien or in procuring its payment or discharge, shall be due and

12. ASSIGNMENT AND SUBLETTING.

12.1 Assignment or Sublease. Tenant shall not, directly or indirectly, assign, transfer, mortgage, pledge, hypothecate or encumber this Lease or any interest therein, nor permit the Leased Premises to be occupied by anyone other than Tenant or sublet the whole or any part of the Leased Premises, nor shall this Lease or any interest hereunder be assignable or transferable by operation of law or by any process or proceeding of any court, or otherwise, without the prior written consent of Landlord.

Notwithstanding the foregoing, Tenant shall be permitted to assign this Lease, or sublet the Leased Premises without landlord's consent to an affiliate of Tenant (affiliate meaning an entity which controls Tenant, is controlled by tenant, or under common control with Tenant, including any subsidiary or parent of Tenant), or to a corporation resulting from a merger or consolidation with Tenant, or to any person or entity which acquires substantially all of the assets of Tenant, or to any person or entity which acquires substantially all of the stock of Tenant. Following any assignment or sublease pursuant to this paragraph, Tenant will remain liable hereunder. The public sale or transfer of the common stock of Tenant shall not constitute an assignment under this Lease.

If Tenant desires at any time to enter an assignment of this Lease or a sublease of the Leased Premises or any portion thereof, where Landlord's consent is required, Tenant shall first give written notice to Landlord of Tenant's desire to do so, which notice shall contain (a) the name of the proposed assignee or subtenant, (b) the proposed merchandising plan for the assignee's or subtenant's business to be carried on in the Leased Premises in accordance with the uses permitted under Section 5 hereof, (c) the terms and provisions of the proposed assignment or sublease, (d) such financial information and past merchandising experience as Landlord may reasonably request concerning the proposed assignee or subtenant, including a resume of the principals of the proposed assignee or subtenant, and (e) a check made payable to the order of Landlord for Seven Hundred Fifty and No/100 Dollars (\$750.00) as a deposit toward Landlord's costs incurred in conjunction with the processing and documentation of the proposed assignment or sublease. Tenant agrees to reimburse Landlord for Landlord's reasonable attorneys' fees incurred in conjunction with the processing and documentation of any such requested transfer, assignment, subletting, licensing or concession agreement, change of ownership or hypothecation of this Lease or Tenant's interest in the Leased Premises, such costs and attorneys' fees not to exceed \$1,000. Tenant shall provide Landlord promptly with fully executed copies of all assignments, subleases and related instruments. No consent by Landlord to any assignment or sublease by Tenant shall relieve Tenant of any obligation to be performed by Tenant under this Lease, whether arising before or after the assignment or sublease. The consent by Landlord to any assignment or sublease shall not relieve Tenant of the obligation to obtain Landlord's express written consent to any other assignment or sublease.

12.2. Consent/Recapture. If Landlord's consent is requested for an assignment or sublease of all or any portion of the Leased Premises, Landlord shall have the right to terminate

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the Lease with respect to that portion of the Leased Premises unless Tenant revokes Tenant's notice of proposed Transfer by notice to Landlord within ten (10) days after acceptance or refusal of Landlord's notice of termination. Landlord shall have the right at its option to enter into the relationship of landlord and tenant with the proposed assignee or subtenant based upon the rent and other economic consideration agreed to by such proposed assignee or subtenant and otherwise upon the terms and conditions of this Lease insofar as applicable to such portion of the Leased Premises.

12.3 Recapture. [omitted]

12.4. Increase in Minimum Rent. In the event that Landlord is required and Landlord consents to a transfer, the monthly Minimum Rent shall be increased on the effective date of the transfer to an amount equal to the average total monthly Minimum Rent and Percentage Rent payable by Tenant during the thirty-six (36) months prior thereto (or such shorter period as may have occurred since the Commencement Date). If the Minimum Rent is increased hereunder, there shall be a proportionate adjustment to the Breakpoint.

12.5 Guarantor of Lease. [omitted]

13. COMMON AREAS AND FACILITIES.

13.1 General. The term "Common Area" refers to all areas within the exterior boundaries of University Village (exclusive of buildings and sites reserved for future buildings) which are now or hereafter made available for general use, convenience and benefit of Landlord and other persons entitled to occupy space in University Village, which areas shall include, but not be limited to, parking areas, driveways, mall, sidewalks, landscaped and planted areas. "Common Area" shall also include all on-site and off-site areas and facilities, which may not be accessible to tenants or other persons, which are used in connection with the operation, management, repair or maintenance of University Village, including janitorial closets, management offices and maintenance areas, storm and sanitary sewer systems, utility lines, disposal plants, lift stations, and retention ponds or basins, whether located within or outside of University Village.

The Common Areas may, at Landlord's election, include areas in adjoining properties which are or become available to Landlord, tenants, employees and invitees of University Village and which are maintained with the Common Area under any reciprocal easement agreement, operating agreement or other such agreement now or hereafter in effect. Without limiting the generality of the foregoing, the Common Area may include, as designated by Landlord from time to time, any parking areas and structures (whether in tiers or at, above or below grade), mall enclosures and roofs covering University Village buildings, entrances, sidewalks, streets or roadways, passageways, concourses, courts, arcades, service corridors, loading platforms and truck docks, delivery areas, escalators and elevators, ramps, stairs, landscaped and vacant areas, pedestrian bridges, skywalks, skybridges, arrival zones, public bathrooms, information and telephone booths, directory signs and equipment, common lighting facilities, drainage areas, lounges and shelters, package pick-up stations, drinking fountains, public comfort and first aid

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stations, public meeting rooms, auditoriums, bus stops, taxi stands, and all furniture, decorations, fixtures, improvements, Systems and Equipment, and other facilities, located in or serving any of the foregoing, except to the extent reserved for use by one or more designated tenants.

13.2 Control and Maintenance of Common Area by Landlord. Landlord shall at all times have the exclusive control and management of the Common Area. Landlord shall keep or cause to be kept the Common Area in a neat, clean, and orderly condition, properly lighted and landscaped, in a first class condition consistent with other upscale regional shopping centers, and shall repair any damage thereto. With respect to the Common Area, Landlord shall have the right from time to time to: employ personnel; establish, modify and enforce reasonable rules and regulations governing the use thereof; construct, maintain and operate lighting facilities; patrol the Common Area; change the area, level, location and arrangement of parking areas and other facilities; restrict parking by Tenant, its officers, agents and employees to employee parking areas; enforce parking charges (by operation of meters or otherwise), with appropriate provisions for free parking ticket validating by Tenant; close all or any portion of the Common Area to such extent as may, in the opinion of Landlord's counsel, be legally sufficient to prevent a dedication thereof or the accrual of any interest therein by any person or the public; close temporarily all or any portion of the parking areas or facilities; discourage non-customer parking; and do and perform such other acts in and to the Common Area as, in the use of good business judgment, Landlord shall determine to be advisable with a view to the improvement of the convenience and use thereof by tenants of University Village, their employees, invitees and customers. Landlord agrees not to place any permanent or temporary kiosks, carts, automatic teller machines ("ATM"), telephones or any other obstructions within an area extending fifteen (15) feet from each of the side demising lines of the Leased Premises, except for customer amenities in the pedestrian sidewalk areas including landscape pots, sidewalk lamppost lighting, landscape "hanging pots", pedestrian moveable signage, customer benches and trash receptacles as are typically found in University Village. If Landlord violates the foregoing prohibition and such violation continues for a period of ten (10) days following written notice from Tenant to Landlord, then Tenant shall be entitled to an abatement of Minimum Rent, Percentage Rent and Other Charges for each day such violation continues.

The other provisions notwithstanding, neither Landlord nor its agents shall be responsible for any law enforcement activities within University Village, and Landlord's employment of security agencies, personnel, or devices, or any other instrumentalities or agents which are intended to deter criminal activity within University Village shall not be deemed to create any such responsibilities for Landlord. Tenant shall be responsible for the protection of its property and, to the extent required by law or as it further deems appropriate, the property of its customers, from theft, vandalism and similar acts.

13.3 License. All Common Area which Tenant may be permitted to use and occupy shall be used and occupied under a revocable license. If the amount of such areas or facilities be diminished, such diminution shall not be subject to any liability, nor shall Tenant be entitled to any compensation or diminution or abatement of rent.

13.4 Additional Land. Subject to Section 4.4(c), should Landlord acquire any interest

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in land not shown as part of University Village on Exhibit B and make the same available for parking or other Common Area purposes, then the operating costs of the Common Area shall also include all of the costs and expenses incurred and paid in connection with such additional land, other than the costs and expenses of acquiring the same.

13.5 Rules and Regulations. Tenant shall comply with the rules and regulations that Landlord may from time to time promulgate and/or modify regarding use and operation of the Common Area. The rules and regulations shall be binding upon Tenant upon delivery of a copy thereof to Tenant. Landlord shall not be responsible to Tenant for the nonperformance of such rules and regulations by any other tenants or occupants of space in University Village. Landlord shall exercise reasonable efforts to enforce the rules of University Village uniformly.

13.6 Employee Parking. It is understood that the employees of Tenant employed at the Leased Premises and the other tenants of Landlord within University Village may not park their motor vehicles in the parking areas of the Common Area which may from time to time be designated for patrons of University Village. Landlord may furnish or cause to be furnished, but shall not be obligated to furnish, space for employee automobile parking. Nothing contained herein shall be deemed to impose liability upon Landlord for personal injury or theft or damage to any motor vehicle or for loss of property from within any motor vehicle, which is suffered by Tenant's employees, customers, service suppliers or other invitees in connection with their use of any parking area. Landlord at all times shall have the right to designate the particular parking areas to be used by any or all of such employees and any such designation may be changed from time to time. Tenant and its employees shall park their automobiles only in those portions of the Common Area, if any, designated for that purpose by Landlord. Tenant shall comply with any system or procedure developed by Landlord, including but not limited to the use of identification stickers, to identify the automobiles of Tenant's employees. If Tenant or its employees fail to park their automobiles in designated parking areas, then Landlord may charge Tenant a fee of Ten and No/100 Dollars (\$10.00) per day for each day or partial day per vehicle parked in any areas other than those designated; provided, however, for the first violation during any calendar year for each Tenant or employee, Landlord will give Tenant written notice and reasonable time during the day the violation occurs to move the vehicle to a permitted parking area and, if the vehicle is promptly moved to a permitted parking area, no fee will be charged. After notice of the first such violation by Tenant or such employee during each calendar year, no notice of any subsequent violation by the same person shall be required prior to the imposition of any parking fine. All amounts due under the provisions of this Section shall be payable by Tenant within twenty (20) days after demand therefor. A Tenant or an employee of Tenant who is using the facilities of University Village as a customer during time periods other than the work shift during which the employee is on-duty may leave on the dashboard of his or her motor vehicle a legible notice which indicates that such person is shopping in University Village. If a Tenant receives a violation notice with respect to the Tenant or an employee who was shopping during a time other than during such employee's work shift and if the Tenant or the employee placed the notice on the dashboard as provided above, the fine shall be rescinded if Tenant so notifies Landlord prior to 5:00 p.m. on the next weekday following receipt of the notice of violation. Any vehicle of a Tenant or an employee of Tenant parked in areas of the Common Area not designated for employee parking may be removed by Landlord and the expense thereof charged to the owner of

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the vehicle. The failure of any employee to park in an appropriate employee parking area shall not be a default by Tenant under this Lease. Tenant shall use its best efforts to cause its employees employed at the Leased Premises to park their personal motor vehicles only in designated employee parking areas. In the event Landlord provides remote parking for Tenant's employees, Landlord shall provide all transportation which may be reasonably required by Tenant's employees with respect to such parking areas. Landlord will cause all employee parking areas (adjacent or remote) to be lit for a period of one (1) hour after the close of University Village and will provide security for such areas.

14. INSURANCE AND INDEMNITY.

14.1 Indemnification. Landlord shall not be liable for injury to any person, or for the loss of or damage to any property (including property of Tenant) occurring in or about the Leased Premises from any cause whatsoever, except to the extent of Landlord's gross negligence or willful misconduct or the gross negligence or willful misconduct of Landlord's employees, agents or contractors. Landlord shall not be responsible or liable to Tenant for any loss or damage which may be occasioned by the acts or omissions of third parties or persons occupying space adjoining the Leased Premises or any part of University Village or by theft or by any act or neglect of any tenant or occupant of University Village. Tenant hereby indemnifies and holds Landlord harmless from and against and agrees to defend Landlord against any and all claims, charges, liabilities, obligations, penalties, damages, costs and expenses (including reasonable attorneys' fees) arising, claimed, charged or incurred against or by Landlord from any matter or thing arising from Tenant's use of the Leased Premises, the conduct of its business or from any activity, work or other things done, permitted or suffered by the Tenant in or about the Leased Premises, and Tenant shall further indemnify and hold harmless Landlord from and against any and all claims arising from any breach or default in the performance of any obligation on Tenant's part or to be performed under the terms of this Lease, or arising from any act or negligence of the Tenant, or any officer, agent, employee, or while within the Leased Premises, guest, or invitee of Tenant, and from all costs, reasonable attorneys' fees, and liabilities incurred in or about the defense of any such claim or any action proceeding brought thereon and in case any action or proceeding be brought against Landlord by reason of such claim. Tenant, upon notice from Landlord, shall defend the same at Tenant's expense by counsel reasonably satisfactory to Landlord. In the event of concurrent negligence of Tenant, its agents, employees, sublessees, invitees while within the Leased Premises, licensees or contractors on the one hand, and that of Landlord, its partners, directors, officers, agents, employees, or contractors on the other hand, which concurrent negligence results in the injury or damage to persons or property and relates to the construction, alteration, repair, addition to, subtraction from, improvement to or maintenance of the Leased Premises, Common Areas or buildings, Tenant's obligation to indemnify Landlord as set forth in this Section shall be limited to the extent of Tenant's negligence, and that of its agents, employees, sublessees, invitees, while within the Leased Premises, licensees or contractors, including Tenant's proportional share of costs, and reasonable attorneys' fees and expenses incurred in connection with any claim, action or proceeding brought with respect to such injury or damage. Tenant hereby agrees to waive its immunity under Industrial Insurance with respect to Landlord. Tenant and Landlord further agree that this indemnification provision was specifically negotiated and agreed to by the parties hereto. None

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of the events or conditions set forth in this Section shall be deemed a constructive or actual eviction or entitle Tenant to any abatement or reduction of rent. Tenant's indemnification obligation pursuant to this paragraph shall survive the expiration or termination of this Lease.

Landlord shall indemnify and hold Tenant harmless from and against and agrees to defend Tenant against any and all claims, charges, liabilities, obligations, penalties, damages, costs and expenses (including reasonable attorneys' fees) to the extent arising from any negligence or willful misconduct of Landlord, its employees, agents or contractors in or about the Leased Premises and the University Village, or to the extent arising from any breach or default in the performance of any obligation on Landlord's part to be performed under the terms of this Lease, including all costs, attorneys' fees, and liabilities incurred in the defense of any such claim, action or proceeding. In addition, except for instances of negligence or willful misconduct of Tenant or its agents, employees, or contractors, Landlord indemnifies and agrees to hold Tenant harmless from and against any and all claims, charges, liabilities, obligations, penalties, damages, costs and expenses (including reasonable attorneys fees) arising, claimed, charged or incurred against or by Tenant from any matter or thing occurring in or about or relating to the common areas of University Village. Landlord's indemnification obligation pursuant to this paragraph shall survive the expiration or termination of this Lease.

14.2 Insurance. During the entire Lease Term, Tenant shall, at its sole cost and expense pay for and keep in full force and effect: (a) an occurrence form Commercial General Liability policy, to indemnify both Landlord and Tenant against any such claims, demands, losses, damages, liabilities and expenses, including insurance against assumed or contractual liability under this Lease, with respect to the Leased Premises and operations of Tenant and any person or entity conducting business in, on or about the Leased Premises for the Tenant or on the Tenant's behalf, in which the limits with respect to liability and property damage shall not be less than \$2,000,000 each occurrence nor less than \$4,000,000 annual aggregate on a location basis; (b) product liability coverage, including, without limitation (if this Lease covers premises in which food and/or alcoholic beverages are sold and/or consumed) liquor liability coverage of not less than \$1,000,000 per occurrence nor less than \$2,000,000 general aggregate on a location basis; (c) special perils form of property insurance, written at replacement cost value in an adequate amount to avoid coinsurance, insuring Tenant's furniture, fixtures, equipment and inventory, including property of Tenant's customers located on the Leased Premises, boiler and machinery coverage, if applicable.

All policies of insurance required to be carried by Tenant pursuant to this Section 14.2 shall be written by responsible insurance companies with a Best rating of at least A-XI. Any such insurance required of Tenant hereunder may be furnished by Tenant under any blanket policy carried by it or under a separate policy therefor. A copy of each policy evidencing such insurance or a certificate of the insurer certifying that such policy has been issued, providing the coverage required by this Section and containing provisions specified herein, shall be delivered to Landlord prior to the commencement of the term of this Lease and, upon renewals, not less than thirty (30) days prior to the expiration of such coverage. Self-insurance shall be permitted for all insurance required of Tenant under this Lease so long as Tenant maintains net worth of at least \$75,000,000.00.

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Each policy evidencing insurance required to be carried by Tenant pursuant to this Section shall contain the following provisions and/or clauses: (a) cross liability, severability or substantially similar clause; (b) a provision that such policy and the coverage evidenced thereby shall be primary and noncontributing with respect to any policies carried by Landlord, and that any coverage carried by Landlord shall be excess insurance; (c) a provision including Landlord and any other parties in interest designated in writing by Landlord as an additional insured; and (d) a provision that the insurer will not cancel, materially change or fail to renew the coverage provided by such policy without first giving Landlord thirty (30) days prior written notice.

If Tenant fails to maintain the insurance required by this Section 14.2, Landlord may obtain and maintain insurance covering such items and interests. Any premiums paid by Landlord therefor shall be deemed Additional Rent and shall be due immediately upon demand. If, on account of the failure of Tenant to comply with the provisions of this Section, Landlord is deemed a co-insurer by its insurance carrier, then any loss or damage which Landlord shall sustain by reason thereof shall be borne by Tenant and shall be immediately paid by Tenant upon receipt of a bill therefor and evidence of such loss.

14.3 Increase in Insurance Premium. Tenant shall not keep, use, sell or offer for sale in or upon the Leased Premises any article which may be prohibited by the customary forms of extended coverage direct damage insurance policies typically in effect for properties similar to University Village in the greater Seattle area. Tenant shall pay any increase in premiums for casualty and fire (including extended coverage) insurance that may be charged during the Lease Term on the amount of such insurance which may be carried by Landlord on the Leased Premises or the building of which they are a part, resulting from Tenant's occupancy or from the type of merchandise which Tenant stores or sells on the Leased Premises, whether or not Landlord has consented

thereto. In such event, Tenant shall also pay any additional premium on the insurance policy that Landlord may carry for its protection against rent loss through fire or casualty. In determining whether increased premiums are the result of Tenant's use of the Leased Premises, a schedule, issued by the organization setting the insurance rate on the Leased Premises, showing the various components of such rate, shall be conclusive evidence of the several items and charges which make up the casualty and fire insurance rate on the Leased Premises. Landlord shall deliver bills for such additional premiums to Tenant at such times as Landlord may elect, and Tenant shall immediately reimburse Landlord therefor.

14.4 Waiver of Subrogation. Landlord and Tenant hereby mutually release each other from liability and waive all right of recovery against each other for any loss in or about the Leased Premises or University Village, from perils insured against or required to be insured against under all-risk insurance contracts (whether or not such insurance contracts are in force), including any extended coverage endorsements thereof, whether due to negligence or any other cause (and each party shall attempt to obtain a waiver of subrogation endorsement from its insurance company); provided that this Section shall be inapplicable if it would have the effect, but only to the extent it would have the effect, of invalidating any insurance coverage of Landlord or Tenant.

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15. EMINENT DOMAIN.

15.1 Total Taking. If all the Leased Premises are taken by the power of eminent domain exercised by any governmental or quasi-governmental authority, this Lease shall terminate as of the date Tenant is required to vacate the Leased Premises and all Minimum Rent and other rentals and charges due hereunder shall be allocated as of that date. The term "eminent domain" shall include the taking or damaging of property by, through or under any governmental or quasi-governmental authority, and any purchase or acquisition in lieu thereof, whether or not the damaging or taking is by the government or any other person.

15.2 Partial Taking. If more than ten percent (10%) of Tenant's sales area or twenty percent (20%) of the Leased Premises shall be taken or appropriated, this Lease may, at the option of either party, be terminated by written notice given to the other party not more than thirty (30) days after Landlord or Tenant receive notice of the taking or appropriation, and such termination shall be effective as of the date when Tenant is required to vacate any portion of the Leased Premises. In the event that more than twenty percent (20%) of the parking areas or other Common Area of University Village shall be taken or appropriated, then the Landlord may at its option terminate this Lease by written notice given to Tenant within sixty (60) days of the date of such taking. If this Lease is so terminated, all Minimum Rent and other charges due hereunder shall be paid to the date of termination. Whenever any portion of the Leased Premises or Common Area is taken by eminent domain and this Lease is not terminated, Landlord shall at its expense proceed with all reasonable dispatch to restore, to the extent that it is reasonably prudent to do so, the remainder of the Leased Premises and Common Area to the condition they were in immediately prior to such taking, and Tenant shall at its expense proceed with all reasonable dispatch to restore its fixtures, furniture, furnishings, floor covering and equipment to the same condition immediately prior to such taking. From the date Tenant is required to vacate that portion of the Leased Premises taken, the Minimum Rent and Other Charges payable hereunder shall be reduced in the same proportion that the area taken bears to the total area of the Leased Premises prior to taking. Landlord shall not terminate this Lease as a result of a Taking unless the Leases for all other tenants identified as "similarly situated" on Exhibit 15.2 attached hereto which Landlord would be permitted to terminate under the facts and circumstances of the taking and under the terms of said leases shall also be terminated.

15.3 Damages. Landlord reserves all rights to the entire damage award or payment for any taking by eminent domain, and Tenant shall make no claim whatsoever against Landlord for damages for termination of its leasehold interest in the Leased Premises or for interference with its business. Tenant hereby grants and assigns to Landlord any right Tenant may now have or hereafter acquire to such damages and agrees to execute and deliver such further instruments of assignment thereof as Landlord may from time to time reasonably request. Tenant shall, however, have the right to claim from the condemning authority all compensation that may be recoverable by Tenant on account of any loss incurred by Tenant in removing, relocating, and/or loss of Tenant's merchandise, furniture, trade fixtures and equipment or for damage to Tenant's business; provided, however, that Tenant may claim such damages only if they are awarded separately in the eminent domain proceeding and not as part of Landlord's damages.

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16. TENANT'S DEFAULT.

16.1 Default. The occurrence of any one or more of the following events shall constitute a default and breach of this Lease by Tenant.

(a) Vacating the Leased Premises. The vacating or abandonment of the Leased Premises by Tenant or the failure of Tenant to be open for business (except in the event of damage or destruction to the Leased Premises or due to an other event or circumstances affecting Tenant and covered by Section 30.12 which prevents Tenant from conducting any business thereon) as required by any provision of this Lease where such failure shall continue for a period of 24 hours after acceptance or refusal of written notice thereof from Landlord.

(b) Failure to Pay Rent. The failure by Tenant to make any payment of Minimum Rent, Percentage Rent, Other Charges, Additional Rent, or any other payment required to be made by Tenant hereunder, as and when due, where such failure shall continue for a period of ten (10) days after acceptance or refusal by Tenant of written notice thereof from Landlord.

(c) Failure to Perform. The failure by Tenant to observe or perform any of the covenants, conditions or provisions of this Lease to be observed or performed by Tenant, other than those described in Subsections 16.1(a) and (b) above, where such failure shall continue for a period of thirty (30) days after written notice thereof by Landlord to Tenant; provided, however, that if the nature of Tenant's default is such that more than thirty (30) days are reasonably required for its cure, then Tenant shall not be deemed to be in default if Tenant commences such cure within said thirty (30) day period and thereafter diligently prosecutes such cure to completion.

(d) Bankruptcy. The making by Tenant of any general assignment or general arrangement for the benefit of creditors; or the filing by or against Tenant of a petition to have Tenant adjudged a bankrupt, or a petition of reorganization or arrangement under any law relating to bankruptcy (unless, in the case of a petition filed against Tenant, the same is dismissed within sixty (60) days of filing); or the appointment of a trustee or a receiver to take possession of substantially all of Tenant's assets located at the Leased Premises or of Tenant's interest in this Lease, where such seizure is not discharged within thirty (30) days after appointment of such trustee or receiver, or the filing of the petition for the appointment of the same, whichever shall first occur.

(e) **Renewed Default.** The commission by Tenant of any default described in section (b) above a third time and within nine (9) consecutive months following the time that Tenant has been given two prior notices of such a default and has cured the same within the permitted time.

16.2 Remedies in Default. In the event of any such default or breach by Tenant, Landlord may at any time thereafter, with or without notice or demand and without limiting Landlord in the exercise of any other right or remedy which Landlord may have by reason of such default or breach:

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(a) **Terminate Lease.** Terminate Tenant's right to possession of the Leased Premises by any lawful means, in which case this Lease shall terminate and Tenant shall immediately surrender possession of the Leased Premises to Landlord. In such event Landlord shall be entitled to recover from Tenant all past due rents, and other necessary expenses of renovation and alteration of the Leased Premises and commissions paid in re-letting even if paid to Landlord or any affiliate of Landlord; reasonable attorneys' fees; the worth at the time of award by the court having jurisdiction thereof of the amount by which the unpaid rent, Additional Rent, and other charges called for herein for the balance of the Lease Term after the time of such award exceeds the amount of such loss for the same period that Tenant proves could be reasonably avoided; and that portion of any leasing commission paid by Landlord and applicable to the unexpired Lease Term of this Lease. Unpaid installments of rent or other sums shall bear interest from the date due at the Default Rate on the first day of each month, commencing on the date due through the date of payment; or

(b) **Continue the Lease.** Maintain Tenant's right to possession, in which case this Lease shall continue in effect whether or not Tenant shall have abandoned the Leased Premises. In such event Landlord shall be entitled to enforce all Landlord's rights and remedies under this Lease, including the right to recover the Minimum Rent and any other charges as may become due hereunder.

(c) **Reletting.** In the event of a default by Tenant, whether or not Landlord elects to terminate or continue the Lease, Landlord may re-let the Leased Premises in whole or in part to one or more tenants, either in the name of Landlord or as agent for Tenant for a term or terms which may be less or greater than the remainder of the term of the Lease, and may agree to grant concessions, free rent and/or additional improvements in connection with any such re-letting. Landlord may receive rent from such re-letting and apply the same first to any expenses incurred in connection with re-entering, ejecting, removing, re-letting, altering, repairing, redecorating, subdividing or otherwise preparing the Leased Premises for re-letting, including brokerage and reasonable attorneys' fees; secondly, to any indebtedness of Tenant to Landlord other than Minimum Rent or items of Additional Rent payable under the Lease; and third, to the fulfillment of any terms or conditions of the Tenant under the Lease and rent payable hereunder. Tenant shall be liable to Landlord for any deficiency; or

(d) **Other Remedies.** Pursue any other remedy now or hereafter available to Landlord under the laws or judicial decisions of the State of Washington. Landlord shall at all times have the right without prior demand or notice except as required by applicable law to: (i) seek any declaratory, injunctive or other equitable relief, and specifically enforce this Lease or restrain or enjoin a violation of any provision hereof, and Tenant hereby waives any right to require that Landlord post a bond in connection therewith, and (ii) sue for and collect any unpaid Rent which has accrued. Notwithstanding anything to the contrary contained in this Lease, to the extent not expressly prohibited by applicable law, in the event of any default by Tenant, Landlord may terminate this Lease or Tenant's right to possession and accelerate and declare that all Rent reserved for the remainder of the Term shall be immediately due and payable (in which event, Tenant's obligations for Percentage Rent, Taxes, Center Expenses, and Marketing Fund Charge

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herein that would have accrued thereafter shall be projected in the manner described in Section B(1) above; provided the Rent so accelerated shall be reduced by the amount of such loss for the same period that Tenant proves could reasonably have been avoided by Landlord and thereafter discounted in accordance with accepted financial practice at the rate of four percent (4%) per annum to the then present value. Landlord shall use reasonable efforts to mitigate its damages.

16.3 Legal Expenses. If either party is required to bring or maintain any action (including assertion of any counterclaim or cross-claim, or claim in a proceeding in bankruptcy, receivership or any other proceeding instituted by a party hereto or by others), or otherwise refers this Lease to an attorney for the enforcement of any of the covenants, terms or conditions of this Lease, the prevailing party in such action shall, in addition to all other payments required herein, receive from the other party all the costs (including reasonable attorneys' fees) incurred by the prevailing party in the enforcement of the covenants, terms and conditions of this Lease (whether or not an action is instituted) and including any such costs and fees incurred by the prevailing party on appeal.

16.4 Proceedings. The parties waive trial by jury in any action, proceeding or counterclaim brought by either party against the other with respect to any matter arising out of or in any way connected with this Lease or University Village. Any action, suit or proceeding relating to, arising out of or in connection with this Lease or University Village brought by either Landlord or Tenant shall be brought in the King County Superior Court, King County, State of Washington. Tenant hereby waives any objection to jurisdiction or venue in any proceeding before such court and agrees that the same shall be the exclusive venue for any such proceeding.

16.5 Remedies Cumulative - Waiver. Landlord's remedies hereunder are cumulative and the Landlord's exercise of any right or remedy due to a default or breach by Tenant shall not be deemed a waiver of, or to alter, affect or prejudice any right or remedy which Landlord may have under this Lease or by law. Neither the acceptance of rent nor any other acts or omission of Landlord at any time or times after the happening of any event authorizing the cancellation or forfeiture of this Lease, shall operate as a waiver of any past or future violation, breach or failure to keep or perform any covenant, agreement, term or condition hereof or to deprive Landlord of its right to cancel or forfeit this Lease, upon the written notice provided for herein, at any time that cause for cancellation or forfeiture may exist, or be construed so as at any time to stop Landlord from promptly exercising any other option, right or remedy that it may have under any term or provision of this Lease, at law or in equity.

16.6 Waiver of Redemption Right. Tenant expressly waives any and all rights of redemption granted by or under any present or future laws or statutes applicable to the Leased Premises.

17. DEFAULT BY LANDLORD.

17.1 Default by Landlord. Landlord shall not be in default unless Landlord fails to perform obligations required of Landlord within a reasonable time, but in no event shall a reasonable time be earlier than thirty (30) days after written notice by Tenant to Landlord (and to

the holder of any first mortgage or deed of trust covering the Leased Premises whose name and address shall have theretofore been furnished to Tenant in writing) specifying wherein Landlord has failed to perform such obligation; provided, however, that if the nature of Landlord's obligation is such that more than thirty (30) days are required for performance, then Landlord shall not be in default if Landlord or the holder of any such mortgage or deed of trust commences performance within such thirty (30) day period and thereafter diligently prosecutes the same to completion. Tenant further agrees not to invoke any of its remedies under this Lease until such thirty (30) days have elapsed. Tenant's remedies for Landlord's default hereunder shall be limited to damages and/or an injunction to the extent suitable, and the parties agree that Tenant shall not have the right to terminate this Lease except in such cases where termination is Tenant's only suitable remedy.

If Landlord shall fail to make a repair Landlord is required to perform under this Lease, and Landlord shall not commence such repair within thirty (30) days after Tenant gives written notice of such failure, or if Landlord fails to diligently pursue such repair once commenced, then Tenant may perform such repair for the account of and at the expense of Landlord and render a bill to Landlord for such reasonable expense. If Landlord fails to pay the bill within ten (10) days after it is rendered, Tenant may bring suitable legal action to require Landlord to pay the bill. If the final judgment of the action determines that Landlord was obligated to make the repair and that Tenant, in making the repair, incurred a reasonable expense, then Tenant, in addition to its normal remedies, shall be entitled to deduct such expenses from payments of rent and other charges due or to become due in the future under this Lease. The amount which may be deducted shall include interest on the judgment at the statutory interest rate for judgments from the date of the cure to the date of payment.

18. RECONSTRUCTION.

18.1 Reconstruction - Insured Loss. In the event the Leased Premises are damaged by fire or other perils covered by Landlord's insurance, Landlord agrees to forthwith repair same, and this Lease shall remain in full force and effect, except that Tenant shall be entitled to a proportionate reduction of the Minimum Rent and Other Charges from the date of damage and while such repairs are being made until the earlier of (i) the date Tenant reopens for business, or (ii) the time reasonably required to make the repairs required to restore the Leased Premises, such proportionate reduction to be based upon the extent to which the damage and making of such repairs shall reasonably interfere with the business carried on by Tenant in the Leased Premises. If the damage is due to the fault or neglect of Tenant or its employees, there shall be no abatement of rent except to the extent covered by Landlord's insurance. Landlord shall not be required to repair any injury or damage to any leasehold improvements, fixtures or personal property of Tenant. No damages, compensation or claims shall be payable by Landlord for inconvenience, loss of business or other damage arising from repair or restoration of any portion of the Leased Premises or University Village.

If the Leased Premises shall be damaged by fire or casualty and Landlord has the obligation to repair under this Lease, if Landlord fails to repair during the twelve (12) month period after occurrence of the damage, Tenant may cancel this Lease by giving notice of

cancellation within ninety (90) days after the twelve (12) month period expires.

18.2 Uninsured Loss. In the event the Leased Premises are damaged as a result of any cause other than the perils covered by all-risk insurance coverage maintained by Landlord, then Landlord shall forthwith repair the same, but only if the extent of the damage is less than ten percent (10%) of the then full replacement cost of the Leased Premises and of the building of which the Leased Premises are a part. If the damage to the Leased Premises or to the building of which the Leased Premises are a part is greater than ten percent (10%) or more of the then full replacement cost of the Leased Premises or the building, respectively, then Landlord shall have the option: (1) to repair or restore such damage, this Lease continuing in full force and effect, but the Minimum Rent and Other Charges to be proportionately reduced as hereinabove provided in this Section; or (2) give notice to Tenant at any time within sixty (60) days after such damage, terminating this Lease as of the date specified in such notice, which date shall be no more than thirty (30) days after the date of such notice. In the event of giving such notice, this Lease shall expire and all interest of Tenant in the Leased Premises shall end on the date so specified in such notice and the Minimum Rent and Other Charges, reduced by a proportionate reduction, based upon the extent, if any, to which such damage interfered with the business carried on by the Tenant in the Leased Premises, shall be paid up to the date of such termination.

18.3 No Obligation. Notwithstanding anything to the contrary contained in this Section 18, Landlord shall not have any obligation whatsoever to repair, reconstruct or restore the Leased Premises when the damage resulting from any casualty covered under this Section occurs during the last twenty-four (24) months of the Lease Term. If Landlord so elects not to repair or restore during the last 24 months of the Lease, Tenant shall have the right to terminate this Lease within thirty (30) days following notice from Landlord that Landlord does not intend to repair or restore. Landlord shall not have any obligation to make any repairs or replacements of any leasehold improvements, fixtures, or other personal property.

18.4 Partial Destruction of University Village. If fifty percent (50%) or more of the gross leasable area of University Village is damaged or destroyed by fire or other cause, notwithstanding that the Leased Premises may be unaffected by such fire or other cause, Landlord may terminate this Lease and the tenancy hereby created by giving Tenant not less than thirty (30) days prior written notice of Landlord's election; provided, however, that such notice shall be given, if at all, within the sixty (60) days following the date of occurrence of such damage or destruction. Minimum Rent and Other Charges shall be prorated as of the date of such termination. Landlord shall not terminate this Lease as a result of partial destruction of University Village unless the leases for all other tenants identified as "similarly situated" on Exhibit 15.2 attached hereto which Landlord would be permitted to terminate under the facts and circumstances of the partial destruction and under the terms of said leases, shall also be terminated.

19. SUBORDINATION AND ATTORNMENT; MORTGAGEE PROTECTION.

19.1 Subordination - - Notice to Mortgagee. Tenant hereby subordinates this Lease to any existing or future mortgages or deeds of trust on University Village or on any leasehold

interest held by Landlord and to any extensions, renewals, or replacements thereof. At the request of Landlord, Tenant shall promptly execute and deliver all instruments which may be appropriate to subordinate this Lease to any existing or future mortgages or deeds of trust on University Village or on the leasehold interest held by Landlord, and to any extensions, renewals, or replacements thereof, on forms reasonably satisfactory to the lender under such future mortgage or deed of trust; provided that any such subordination agreements also provide that Tenant's possession shall not be disturbed following foreclosure so long as Tenant is not in default hereunder, subject to applicable notice and cure periods expressly provided herein. Notwithstanding anything to the contrary in this Lease, Landlord shall not be in default under any provision of this Lease unless written notice specifying such default is given to Landlord and to all persons who have an interest in all or part of University Village as mortgagees and/or deed of trust beneficiaries, provided that Tenant has been notified in writing (by way of Notice of Assignment of Rents and Leases, or otherwise) of the addresses of such mortgagees or deed of trust holders, and the provisions of Section 17.1 have been complied with. Landlord agrees to use reasonable efforts to obtain from its existing lender, following execution of this Lease by all parties, a Non-Disturbance and Attornment Agreement (which agreement shall be on such lender's standard form and which may also provide additional terms reasonably satisfactory to Tenant regarding subordination of this Lease if required by such lender).

19.2 Tenant's Certificate. Tenant shall at any time and from time to time upon not less than fifteen (15) days prior written notice from Landlord execute, acknowledge and deliver to Landlord a statement in writing (a) certifying that this Lease is unmodified and in full force and effect (or, if modified, stating the nature of such modification and certifying that this Lease as so modified is in full force and effect), and the date to which the rental and other charges are paid in advance, if any, and (b) acknowledging that there are not, to Tenant's knowledge, any uncured defaults on the part of Landlord hereunder, or specifying such defaults if any are claimed, (c) setting forth the date of commencement of rents and expiration of the Lease Term hereof; and (d) setting forth such other information with respect to this Lease as Landlord may reasonably request. Any such statement may be relied upon by any prospective purchaser or encumbrancer of all or any portion of University Village. If Tenant fails to respond to a request hereunder in a timely fashion (but in no event longer than thirty (30) days), Tenant shall be deemed to have admitted the accuracy of any information provided by Landlord to the prospective purchaser or lender and to have certified that this Lease is in full force and effect with no uncured defaults on the part of Landlord; that the security deposit is as stated in the Lease; and that no more than one month's rent has been paid in advance.

19.3 Mortgagee Protection Clause. Tenant agrees to give any mortgagees and/or deed of trust holders, by registered mail, a copy of any notice of default served upon the Landlord, provided that prior to such notice Tenant has been notified in writing (by way of Notice of Assignment of Rents and Leases, or otherwise) of the addresses of such mortgagees or deed of trust holders. Tenant further agrees that if Landlord shall have failed to cure such default within the time provided for in this Lease, then the mortgagees or deed of trust holders shall have an additional thirty (30) days within which to cure such default or if such default cannot be cured within that time, then such additional time as may be necessary if within such thirty (30) days any mortgagee or deed of trust holder has commenced and is diligently pursuing the remedies

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necessary to cure such default (including but not limited to commencement of foreclosure proceedings if necessary to effect such cure), in which event this Lease shall not be terminated if such remedies are being so diligently pursued.

19.4 Ground Lease. [omitted]

20. ACCESS BY LANDLORD.

20.1 Right of Entry. Landlord or Landlord's employees, agents, and contractors shall have the right (upon reasonable notice depending upon the circumstances) to enter the Leased Premises at any reasonable time to examine the same, and to show them to prospective purchasers or during the last six (6) months of the Lease Term tenants of the building, and to make such repairs, alterations, improvements or additions as Landlord may deem necessary or desirable to the Leased Premises or to University Village. If Tenant is not personally present to permit entry and an entry is necessary, Landlord may in case of emergency forcibly enter the same, without rendering Landlord liable therefor. Nothing contained herein shall be construed to impose upon Landlord any duty of repair of the Leased Premises or building of which the Leased Premises are a part except as otherwise specifically provided for herein. Landlord shall exercise its best reasonable efforts to make repairs and alterations to the Leased Premises only during reasonable hours except in the event of an emergency. In connection with the exercise of any of these rights, Landlord agrees that to the extent practicable, Landlord will not interfere with the operation of Tenant's business and will attempt to complete repairs during non-business hours.

20.2 Excavation. If an excavation is made upon property adjacent to the Leased Premises, Tenant shall afford to the person causing or authorized to cause such excavation, license to enter upon the Leased Premises for the purpose of doing such work as Landlord shall deem necessary to preserve the wall of the building of which the Leased Premises is a part from injury or damage and to support the same by proper foundations, without any claim for damages or indemnification against Landlord or diminution or abatement of rent.

20.3 Reserved Areas. Landlord reserves all rights to use (or grant other parties the right to use) and Tenant shall have no right, title or interest in: (i) the roof of any structures, (ii) exterior non-storefront portions of the Leased Premises (including, without limitation, demising walls and outer walls of the area of the building in which the Leased Premises are located), (iii) air rights above the Leased Premises and rights to the land and improvements below the floor level of the Leased Premises, and (iv) areas within the Leased Premises necessary for utilities, services, safety and operation of University Village that will not materially interfere with Tenant's use of the Leased Premises, including any systems and equipment, fire stairways, and space between the suspended ceiling of the Leased Premises and the slab of the floor or roof thereabove. If the Leased Premises does not contain a suspended ceiling, the Leased Premises shall extend vertically to the height where, in Landlord's reasonable opinion, a suspended ceiling would otherwise exist, and Landlord reserves the right to install a suspended ceiling and use the area thereabove. Tenant utilizes a "Frame Relay" service in its operations in connection with its telecommunications system. Landlord shall permit Tenant to install the equipment and facilities necessary to utilize such Frame Relay service for the Leased Premises, including connections

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from Landlord's local exchange carrier's telecommunications facilities at University Village to the Leased Premises, exclusively in connection with Tenant's business, provided that (a) Tenant shall be continuously complying with all governmental laws, ordinances and regulations; (b) upon expiration of the term of this Lease, Tenant shall remove such equipment and facilities and repair all damage caused by installation and removal; (c) Tenant shall indemnify and hold harmless Landlord from any damages, expenses, costs, reasonable attorney's fees, and other costs and expenses arising in connection with the installation,

operation, removal and repair of such equipment and facilities; (d) Tenant shall give Landlord at least thirty (30) days prior written notice of its intention to install such equipment and facilities; (e) Tenant shall comply with all requirements of Landlord's local exchange carrier in connection with the installation of such equipment and facilities; (f) Tenant shall comply with Landlord's construction requirements and criteria as set forth in this Lease, and (g) Tenant shall use its best efforts to minimize interference with the operations of Landlord and other tenants in University Village. In the event of any future changes or modifications in Tenant's telecommunications requirements, Landlord shall not unreasonably withhold its approval of Tenant's installations, including without limitation installations required to connect the Leased Premises to University Village's telecommunications access facilities. Except as to conduits in place as of the date that Tenant takes possession of the Leased Premises, any utility conduits (electrical, HVAC, water, etc.) installed for the benefit of other tenants and running through the Leased Premises shall be installed above Tenant's lowered ceiling, and as close to the back wall of the Leased Premises as possible.

20.4 Remeasurement. Landlord shall remeasure the Leased Premises prior to the date Tenant takes possession of the Leased Premises. All measurements shall be made from the outside of exterior walls, shaft walls or corridors or the center of any common walls, without deduction for columns, stairs or other interior construction or equipment. If such remeasurement determines that the Leased Premises contain a different number of square feet than set forth in Article 1, the Minimum Rent, Breakpoint and Other Charges shall be adjusted retroactively and prospectively on a pro rata basis to reflect the number of square feet determined by such remeasurement; provided, however, that if such measurement reveals that the floor area of the Leased Premises is more than three percent (3%) above the figure therefore set forth in Section 1.4, then such charges hereunder shall nevertheless be increased as aforesaid but only by three percent (3%). Upon either party's request, the revised square footage shall be confirmed in an amendment to this Lease signed by both parties. Landlord shall give Tenant 48 hours prior notice before such remeasurement and Tenant may elect to have a representative of Tenant present during such remeasurement.

20.5 Access to University Village. Landlord may prevent or restrict access to University Village or designated portions thereof by such security procedures as Landlord may from time to time impose on days and hours when University Village is, or portions thereof are, closed for business to the public. Landlord reserves the right to control, prevent access by and remove, any person whose presence in the judgment of Landlord shall be prejudicial to the safety, character, reputation and interests of University Village, or who in the judgment of Landlord, is intoxicated or under the influence of liquor or drugs.

20.6 Emergency Closings. Landlord shall have the right (but not the obligation) to

limit or prevent access to all or any portion of University Village, shut down elevator and escalator service, activate emergency controls or procedures, or otherwise take such action or preventive measures deemed necessary by Landlord for the safety of tenants or other occupants of University Village or the protection of University Village or other property located thereon or therein, in case of fire or other casualty, riot or other civil disorder, strike or labor unrest, public excitement or other dangerous condition, or threat thereof.

20.7 Other Tenants. Landlord reserves the right to lease any portion of University Village to such other tenants as Landlord, in Landlord's sole discretion, deems appropriate, whether or not engaged in the same or similar business for which Tenant is permitted to use the Leased Premises under this Lease. Except as specifically provided herein, Tenant acknowledges that Landlord has made no representations as to the presence of any specific tenant or number or types of tenants at University Village as of or after the Commencement Date, hours or days that such other tenants shall or may be open for business, or gross sales which may be achieved by Tenant or any other tenants at University Village. Except as specifically provided herein, a vacation or abandonment of its premises or cessation of business in University Village by any other tenant or occupant shall not release or excuse Tenant from Tenant's obligations under any provision of this Lease.

21. SURRENDER OR ABANDONMENT OF LEASED PREMISES.

21.1 Surrender of Possession. Tenant shall promptly yield and deliver to Landlord possession of the Leased Premises at the expiration or prior termination of this Lease.

21.2 Holding Over. Any holding over by Tenant after the expiration of the Lease Term hereof, with Landlord's written consent, shall be construed to be a tenancy from month to month at the rents and on all of the terms and conditions set forth herein, to the extent not inconsistent with a month-to-month tenancy; provided, however, monthly Minimum Rent shall be one hundred fifty percent (150%) of the monthly minimum Rent in effect during the calendar month prior to the expiration of the Lease. Notwithstanding the foregoing, Tenant shall not be required to pay the increased Minimum Rent if Landlord and Tenant are engaged in good faith negotiations to extend this Lease and enter into an agreement providing for the same within 45 days after expiration of this Lease.

21.3 Abandonment. Should Tenant vacate or abandon the Leased Premises or be dispossessed by process of law or otherwise, such abandonment, vacation or dispossession shall be deemed a breach of this Lease, and, in addition to any other rights which Landlord may have, Landlord may remove any personal property belonging to Tenant which remains on the Leased Premises and store the same, the cost of such removal and storage to be charged to the account of Tenant.

21.4 Voluntary or other Surrender. The voluntary or other surrender of this Lease by Tenant, or a mutual cancellation thereof, shall not work a merger, but shall, at the option of Landlord, terminate all or any existing subleases or subtenancies, or operate as an assignment to it of any or all such subleases or subtenancies.

22. QUIET ENJOYMENT. Upon fully complying with and promptly performing all of the terms, covenants and conditions of this Lease on its part to be performed, and upon the prompt and timely payment of all sums due hereunder, Tenant shall have and quietly enjoy the Leased Premises for the Lease Term set forth herein.

23. TENANT'S REPRESENTATIONS.

23.1 Corporate Authority. Tenant represents and warrants that the individual(s) executing this Lease on Tenant's behalf is/are duly authorized to execute and deliver this Lease on behalf of said entity, in accordance with a duly adopted resolution of the board of directors or other governing body of such entity, that such action and execution are in accordance with the bylaws or other governing documents of such entity, and that this Lease is binding upon such entity in accordance with its terms.

23.2 Financial Matters. Tenant represents and warrants that there are no proceedings pending, or to the best of Tenant's knowledge, threatened, which would adversely affect the financial condition of Tenant or the ability of Tenant to enter into this Lease, or the validity and enforceability of this Lease; no provision of any mortgage, contract or agreement binding on Tenant which would conflict with or prevent the performance of this Lease by Tenant; that the financial statements of Tenant provided to Landlord are true and correct and prepared in accordance with generally accepted accounting principles consistently applied; and that there have been no material, adverse changes in financial condition of Tenant since the date of such financial statements.

23.3 No Reliance. Tenant acknowledges and agrees that neither Landlord nor any agent or representative of Landlord, including any leasing agent, has made, and Tenant has not relied upon, any representations or assurances as to Tenant's projected or likely sales volume, customer traffic or profitability in the Leased Premises or University Village. Tenant acknowledges that to the extent any projections, materials, discussions, reports or other information relating to sales volume, customer traffic or profitability have been provided to Tenant by Landlord, that the same are not to be construed as a promise, guarantee or representation that Tenant will realize any sales volume, customer traffic or profitability.

24. SIGNS. Tenant shall not place or suffer to be placed on the exterior walls of the Leased Premises or upon the roof or any exterior door or wall or on the exterior or interior of any window thereof any sign, awning, canopy, marquee, advertising matter, decoration, letter or other thing of any kind (exclusive of the signs, if any, which may be provided for in the original construction or improvement plans and specifications approved by the Landlord and Tenant hereunder, and interior signs in accordance with Tenant's national sign program) without the prior written consent of Landlord. Landlord hereby reserves the exclusive right to the use for any purpose whatsoever of the roof and exterior of the walls of the Leased Premises and the building of which the Leased Premises are a part. Notwithstanding anything to the contrary herein, Tenant shall have the right to place reasonably sized, professionally prepared signs and decals consistent with J. Crew's national signage program in Tenant's store windows.

25. DISPLAYS. Tenant may not display or sell merchandise or allow grocery carts or other similar devices within the control of Tenant to be stored or to remain outside the defined exterior walls and permanent doorways of the Leased Premises. Tenant further agrees not to install or use any exterior lighting, amplifiers or similar devices in or about the Leased Premises, such as flashing lights, searchlights, loudspeakers, phonographs or radio broadcasts. If music or any other audio transmission emanating from within the Leased Premises is objectionable or offensive (in the reasonable judgment of Landlord), Landlord may require Tenant to decrease the volume of such sounds to a reasonable level, as determined by Landlord, and Tenant shall comply immediately.

26. AUCTIONS AND SALES.

26.1 General. Tenant shall not conduct or permit to be conducted any sale by auction upon or from the Leased Premises, whether the auction be voluntary, involuntary, pursuant to any assignment for the payment of creditors, or pursuant to any bankruptcy or other insolvency proceeding.

26.2 No Distress Sales. No auction, fire, bankruptcy, "going out of business" or other distress sales of any nature may be conducted on the Leased Premises without the prior written consent of Landlord.

27. MERCHANTS' ASSOCIATION.

27.1 General. Tenant shall become a member of, participate fully in, pay dues to, and remain in good standing in the Merchants' Association for University Village. Tenant will further abide by the bylaws, regulations and rules of the Merchants' Association. The sole objectives of the Association shall be (i) to promote and advertise University Village as an entity through cooperative advertising efforts, relying on assistance from the Landlord's representative in promoting University Village, (ii) to encourage its members to deal fairly and courteously with their customers, and (iii) to encourage ethical business practices. The Merchants' Association shall not act or attempt to function as a collective body for the purpose of engaging in discussions or advice concerning management, leasing, or other administrative functions of University Village nor shall it exercise any control over the Common Area or sponsor or hold any activities in or on behalf of University Village other than through the Landlord and with the Landlord's prior approval.

27.2 Board of Directors. The Merchants' Association is governed by a Board of Directors elected by the members of the Merchants' Association with the number of such board members being determined from time to time in accordance with its bylaws. Landlord, the major department store tenant, the major drug store tenant, the major hardware store tenant and the major supermarket tenant may not be denied membership on the Board of Directors.

27.3 Dues. Tenant shall pay an annual Promotional Assessment in the amount of \$0.50 per square foot of the ground level portion of the Area of Leased Premises.

27.4 Method of Payment; Annual Adjustment. The Tenant shall pay its Promotional Assessment in monthly installments, payable in advance on the first day of each month during the calendar year. Tenant's assessment shall be adjusted bi-annually on the first day of every second calendar year after 2004 ("Adjustment Date") during the term of this Lease by adjusting the amount per square foot set forth in Section 27.3 above for any increase in the cost of living index for December 2004 as compared to the index for the December immediately preceding each Adjustment Date. Adjustments shall be based upon the U.S. city Average Consumer Price Index for Urban Wage Earners and Clerical Workers for All Items (1982-84 = 100) published by the bureau of Labor of the U.S. Department of Labor as published for December 2004 and as published for the month of December immediately preceding the Adjustment Date. If the index ceases to be published or is modified, such increase shall be based on the replacement index and/or such adjustment factors as provided by the bureau, or otherwise upon a reasonably comparable cost of living index. Notwithstanding the foregoing, in no event shall the Promotional Assessment increase by more than six percent (6%) every two years on a non-cumulative basis.

27.5 Landlord's Contribution. Landlord shall be a member of the Merchants' Association and shall pay, on a noncumulative basis, a contribution equal to twenty-five percent (25%) of all contributions collected by the Merchants' Association; provided, however, that the Landlord's contribution shall not exceed the sum of Fifty Thousand and No/100 Dollars (\$50,000) in any one (1) fiscal year. Landlord may elect to contribute part or all of the services of a marketing director in lieu of all or a portion of its cash contribution. In the event Landlord makes the above election, the marketing director shall be under the exclusive control and supervision of Landlord.

27.6 Use of Tenant's Name. Landlord covenants that it will not advertise the Tenant's business or its merchandise in any media without first obtaining Tenant's consent, which consent may be withheld in Tenant's sole discretion.

27.7 Conversion to Marketing Fund. At any time during the Term of this Lease, Landlord shall have the right to disband the Merchants' Association by written notice to each member thereof. In lieu of the Merchants' Association, Landlord shall establish a Marketing Fund to furnish and maintain advertising and sale promotions, which, in Landlord's sole opinion, will benefit University Village. The Marketing Director, staff and any consultants shall be hired by the Landlord to direct and perform the activities of the Marketing Fund and shall be under the exclusive control and supervision of Landlord. Tenant's advertising requirements under the Marketing Fund shall be the same as those under the Merchants' Association as provided above. Landlord shall appoint a committee comprised of a representative from each of four tenants occupying premises in University Village to review the advertising and other promotional activities provided by the Marketing Fund. During each Lease Year, Tenant shall pay to Landlord in equal monthly installments, as its share of the cost of the Marketing Fund, an amount herein equal to the then current Merchants' Association dues payable by Tenant in accordance with this Section 27. Tenant's obligations to participate in the Marketing Fund and pay its share of the costs are subject to the same conditions and caps as Tenant's obligations to participate in

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and pay its share of funding the Merchant's Association.

28. MAJOR RENOVATION.

28.1 Cooperation of Tenant. [omitted]

28.2 Construction Coordination. If Landlord shall undertake an expansion and/or reconfiguration of University Village, in whole or in part, such construction and reconfiguration may result in noise, dust, debris and other disruption which could adversely impact Tenant's business in the Leased Premises. Landlord shall use reasonable efforts to mitigate the adverse impact on Tenant, including any adverse affect on access to or visibility of Tenant's storefront and the Leased Premises, but Tenant understands and accepts that such impacts may not be capable of mitigation without unreasonable expense. Such adverse impacts shall not constitute a default under this Lease by Landlord or a constructive eviction of Tenant. In connection with such a project, Landlord may find it necessary or desirable, as determined by Landlord, to enter into the Leased Premises to inspect the same or perform work in or around the Leased Premises, including, without limitation, the installation of temporary and/or permanent supports and other structures and facilities, provided the installation of same shall not materially adversely affect Tenant's ability to operate its business in the Leased Premises for the Permitted Use, no such installations shall be made in the sales area of the Leased Premises unless no other reasonable alternative is available and Landlord shall use reasonable efforts to perform any such work in the Leased Premises during non-business hours. If, as a result of no other reasonable alternative being available, Landlord notifies Tenant of its intention to install a column or columns in the sales area of the Leased Premises in connection with such a project, Tenant shall have the right, upon one hundred twenty (120) days notice to Landlord delivered within twenty (20) days of receipt of such notice from Landlord, to terminate this Lease, unless within sixty (60) days following Landlord's receipt of Tenant's notice of termination, Landlord delivers notice to Tenant advising Tenant of its decision to not proceed with the installation of any columns within the Leased Premises. Tenant consents to such actions by Landlord and Landlord's agents and contractors.

29. HAZARDOUS AND TOXIC SUBSTANCES.

29.1 Tenant's Representation and Warranty. Tenant represents, warrants and covenants that throughout the term of this Lease, no chemical, substance, material or waste or component thereof which is now or hereafter listed, defined or regulated as a hazardous or toxic chemical, substance, material or waste or component thereof by any federal, state or local governing or regulatory body having jurisdiction, or which would trigger any employee or community "right-to-know" requirements adopted by any such body ("Hazardous Substances") will be improperly generated, treated, released, stored or disposed of, or otherwise deposited in or on the Leased Premises by Tenant, its employees, agents, contractors, subtenants, licensees or invitees, including without limitation the surface waters and subsurface waters thereof, no underground tanks will be located on the Leased Premises, and there will be no Hazardous Substances or hazardous conditions in or on the Leased Premises which may support a claim or cause of action under any federal, state or local environmental statutes regulations, ordinances or

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regulatory requirements. Tenant may store in the Leased Premises household quantities of cleaning supplies provided Tenant uses care in storing them and otherwise complies with all applicable laws.

29.2 Tenant's Notice to Landlord. Tenant shall promptly notify Landlord of: (i) any enforcement, cleanup or other regulatory action taken or threatened by any governmental or regulatory authority with respect to the presence of any Hazardous Substances on the Leased Premises or the migration thereof from or to other property, (ii) any demands or claims made or threatened by any party relating to any loss or injury resulting from any Hazardous Substances on the Leased Premises, (iii) any release, discharge or nonroutine, improper or unlawful disposal or transportation of any Hazardous Substances on or from the Leased Premises or in violation of this Section 29, and (iv) any matters where Tenant is required by law to give a notice to any governmental or regulatory authority respecting any Hazardous Substances on the Leased Premises. Landlord shall have the right (but not the obligation) to join and participate, as a party, in any legal proceedings or actions affecting the Leased Premises initiated in connection with any environmental, health or safety law.

29.3 Remediation of Contamination. If any Hazardous Substances are released, discharged or disposed of by Tenant, or their employees, agents or contractors, on or about University Village in violation of the foregoing provisions, Tenant shall immediately, properly and in compliance with applicable laws clean up and remove the Hazardous Substances from University Village and any other affected property and clean or replace any affected personal property, at Tenant's expense. Such clean up and removal work shall be subject to Landlord's prior written approval (except in emergencies), and

shall include, without limitation, any testing, investigation, and the preparation and implementation of any remedial action plan required by any court or governmental body having jurisdiction or reasonably required by Landlord. If Landlord or any lender to Landlord or any governmental body arranges for any tests or studies showing that this Section has been violated, Tenant shall pay for the costs of such tests.

29.4 Indemnity of Landlord. Tenant shall defend, indemnify, and hold Landlord harmless from all claims, liabilities, damages, costs, expenses fees fines and penalties (both civil and criminal) (including, but not limited to, reasonable attorneys' fees) resulting from any personal injury, property damage, water pollution, air pollution, hazardous waste combination, Hazardous Substances contamination, damage to fish or wildlife, damage to natural resources, or environmental harm due to the release, discharge or disposal of Hazardous Substances by Tenant or Tenant's employees, agents or contractors on or about University Village. Without limiting the generality of the foregoing, Tenant's obligations under this subsection shall extend to liability arising under common law or under any federal, state, local, or other governmental requirement. This indemnity shall apply to the fullest extent permitted by applicable law. Tenant's indemnification obligation pursuant to this paragraph shall survive the expiration or termination of this Lease.

29.5 Acceptance of Leased Premises. Tenant accepts the Leased Premises "AS IS" subject only to completion of Landlord's Work.

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29.6 Soil Contamination. In the event that any preexisting contamination in the soils beneath the building in which the Leased Premises are located and affecting the construction or use of the Leased Premises is discovered following the date of this Lease, and if the same requires remediation pursuant to any applicable law, rule, regulation or order of any governmental agency having jurisdiction over the same, or otherwise in the judgment of Landlord, then, Landlord shall promptly remediate the same at Landlord's sole cost and expense and, if Landlord is required to enter into the Leased Premises or if such remediation measures require the disruption of Tenant's use of the Leased Premises, the parties agree that to the extent that Tenant is unable to use the Leased Premises for Permitted Uses under this Lease, the Minimum Rent and Other Charges payable by Tenant hereunder shall equitably abate in proportion to the extent of the Leased Premises so affected for the period of any such interruption.

29.7 Indemnity of Tenant. To the best of Landlord's knowledge, there are no Hazardous Substances, including, without limitation, any asbestos containing materials, located within or under the Leased Premises. Landlord shall defend, indemnify, and hold Tenant harmless from all claims, liabilities, damages, costs, expenses, fees, fines and penalties (both civil and criminal) (including, but not limited to, reasonable attorneys' fees) resulting from any personal injury, property damage, water pollution, air pollution, hazardous waste contamination, Hazardous Substances contamination, damage to fish or wildlife, damage to natural resources, or environmental harm due to preexisting contamination of the Leased Premises by Hazardous Substances (except to the extent such Hazardous Substances are within the Leased Premises due to acts by Tenant or Tenant's employees, agents or contractors on or about University Village). Landlord's indemnification obligation pursuant to this paragraph shall survive the expiration or termination of this Lease.

30. MISCELLANEOUS.

30.1 Successors or Assigns. All the terms, conditions, covenants and agreements of this Lease shall extend to and be binding upon Landlord, Tenant and their respective heirs, administrators, executors, successors and assigns, and upon any person or persons coming into ownership or possession of any interest in the Leased Premises by operation of law or otherwise, and shall be construed as covenants running with the land.

30.2 Tenant Defined. The word "Tenant" as used herein shall mean each and every person, partnership or corporation who is mentioned as Tenant herein or who executes this Lease as Tenant.

30.3 Broker's Commission. Landlord and Tenant represent and warrant that it has incurred no liabilities or claims for brokerage commissions or finder's fees in connection with the execution of this Lease and that it has not dealt with or has any knowledge of any real estate broker, agent or salesperson in connection with this Lease. Each party agrees to indemnify and hold the other harmless from all such liabilities or claims (including, without limitation, attorneys' fees).

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30.4 Partial Invalidity. If any term, covenant, or condition of this Lease or the application thereof to any person or circumstance is, to any extent, invalid or unenforceable, the remainder of this Lease, or the application of such term, covenant or condition to persons or circumstances other than those as to which it is held invalid or unenforceable, shall not be affected thereby and each term, covenant or condition of this Lease shall be valid and be enforced to the fullest extent permitted by law. Titles of sections and paragraphs herein are for convenience only and shall not affect the meaning or interpretation of any provision of this Lease.

30.5 Recording. Tenant shall not record this Lease without the prior written consent of Landlord. However, upon the request of Landlord, both parties shall execute a memorandum or "short form" of this Lease for the purposes of recordation in a form customarily used for such purposes. Said memorandum or short form of this Lease shall describe the parties, the Leased Premises and the Lease Term and shall incorporate this Lease by reference.

30.6 Notices. Any notices required in accordance with any of the provisions herein shall be in writing and, if to Landlord, shall be delivered or mailed by registered or certified mail or reputable air courier such as Federal Express to the address of Landlord as set forth at the beginning of this Lease or at such other place as Landlord may in writing from time to time direct to Tenant, and if to Tenant, shall be delivered or mailed by registered or certified mail or reputable air courier such as Federal Express to Tenant at 770 Broadway, New York, NY 10003, Attn: General Counsel. If there is more than one Tenant, any notice required or permitted hereunder may be given by or to any one thereof and shall have the same force and effect as if given by or to all thereof. Notice shall be deemed delivered upon acceptance or refusal of the same.

30.7 Waiver. The waiver by Landlord or Tenant of any term, covenant or condition herein contained shall not be deemed to be a waiver of such term, covenant or condition or any subsequent breach of the same or any other term, covenant or condition herein contained. The subsequent acceptance of Minimum Rent or Percentage Rent or any other charges or sum hereunder by Landlord shall not be deemed to be a waiver of any preceding default by Tenant of any term, covenant or condition of this Lease, other than the failure of Tenant to pay the particular sum so accepted, regardless of Landlord's knowledge of such preceding default at the time of the acceptance of such sum.

30.8 Joint Obligation. If there be more than one Tenant, the obligations hereunder imposed shall be joint and several.

30.9 Time. Time is of the essence of this Lease and each and all of its provisions in which performance is a factor.

30.10 Late Charges. If Tenant fails to pay, when the same is due and payable, any Minimum Rent or Percentage Rent or Additional Rent, or the Other Charges described herein, such unpaid amounts shall bear interest at Default Rate on the first day of each month, commencing on the date due to the date of payment. In addition to such interest, Tenant

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acknowledges that either the late reporting of gross sales or late payment by Tenant of any monthly installment of Minimum Rent, Percentage Rent or Other Charges will cause Landlord to incur certain costs and expenses not contemplated under this Lease, the exact amount of such costs being extremely difficult or impractical to fix. Such costs and expenses will include, without limitation, administrative and collection costs, and processing and accounting expenses. Therefore, if any gross sales or any installment of Minimum Rent, Percentage Rent or Other Charges is not received by Landlord from Tenant within ten (10) days after Landlord has given written notice of such delinquency to Tenant, Tenant shall immediately pay to Landlord a late charge of Two Hundred and No/100 Dollars (\$200.00) for each delinquency. Landlord and Tenant agree that this late charge represents a reasonable estimate of such costs and expenses and is fair compensation to Landlord for its loss suffered by such nonpayment by Tenant. Acceptance of this late charge shall not constitute a waiver of Tenant's default with respect to such nonpayment by Tenant nor prevent Landlord from exercising all other rights and remedies available to Landlord under this Lease. Landlord shall apply payments made by Tenant first to accrued charges, interest and rent in the following order: Late Charges, interest, Minimum Rent, Percentage Rent, Other Charges and Additional Rent; and any balance remaining to current Minimum Rent, Percentage Rent, Other Charges and Additional Rent.

30.11 Prior Agreements. This Lease contains all of the agreements of the parties hereto with respect to any matter covered or mentioned in this Lease, and no prior agreements or understanding pertaining to any such matters shall be effective for any purpose. No provisions of this Lease may be amended or added to except by an agreement in writing signed by the parties hereto or their respective successors in interest. This Lease shall not be effective or binding on any party until fully executed by both parties hereto.

30.12 Inability to Perform. Except for the obligation of the Tenant to pay Rent, which shall not be excused by force majeure, this Lease and the obligations of the parties hereunder shall be excused for the period of a delay in performing its obligations hereunder, if such inability or delay is caused by reason of strike, labor troubles, acts of God, or any other cause beyond the reasonable control of the obligated party.

30.13 Choice of Law. This Lease shall be governed by the laws of the State of Washington.

30.14 Landlord's Consent. Except as otherwise specifically provided herein, whenever Landlord's consent or approval is required, the same may be withheld in Landlord's sole discretion.

30.15 Negotiations. This Lease, and any Riders and Exhibits hereto, have been mutually negotiated by Landlord and Tenant, and any ambiguities shall not be interpreted in favor of either party. Any printed provisions that have been deleted shall not be used to interpret the remaining provisions.

30.16 Landlord's Liability. Anything in this Lease to the contrary notwithstanding, the covenants, undertakings and agreements herein made on the part of Landlord are made and

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intended not as personal covenants, undertakings and agreements for the purpose of binding Landlord personally or the assets of Landlord, but are made and intended for the purpose of binding only Landlord's interest in the Leased Premises and University Village, as the same may from time to time be encumbered. In consideration of the benefits accruing hereunder, Tenant and all successors and assigns, covenant and agree that in the event of any actual or alleged failure, breach or default hereunder by Landlord, the sole and exclusive remedy of Tenant hereunder shall be against the Landlord's interest in the Leased Premises and University Village, and no general or limited partner of Landlord, or any director, officer, agent or employee of any corporation which is the Landlord or a general or limited partner of Landlord, shall be sued or named as a party in any such suit or action and no judgment shall be taken against any such general or limited partner of Landlord. In case Landlord or any successor owner of University Village shall convey or otherwise dispose of any portion thereof in which the Leased Premises are located to another party (and nothing herein shall be construed to restrict or prevent such conveyance or disposition), such other party shall thereupon be and become landlord hereunder and shall be deemed to have fully assumed and be liable for all obligations of this Lease to be performed by Landlord, including the return of any Security Deposit. Tenant shall attorn to such other party, and Landlord or such successor owner shall, from and after the date of conveyance, be free of all liabilities and obligations hereunder.

30.17 Conflict. In the event there is a conflict between the terms of this Lease and Exhibits and the plans for Tenant's work approved in writing by Landlord, the approved plans shall prevail.

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IN WITNESS WHEREOF, the parties hereto have executed this instrument the day and year first above set forth.

LANDLORD:

UNIVERSITY VILLAGE LIMITED PARTNERSHIP,
a Washington limited partnership

By: UV, INC.,
a Washington corporation,
Its General Partner

By: /s/ Matt Griffin

TENANT:

GRACE HOLMES, INC.,
a Delaware corporation

By: /s/ Scott Gilbertson

Printed Name: Scott Gilbertson

Title: Chief Operating Officer

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LANDLORD ACKNOWLEDGMENT

STATE OF WASHINGTON)
) ss.
COUNTY OF KING)

On this day of , 2003, before me, the undersigned, a notary public in and for the state of Washington, duly commissioned and sworn personally appeared Stuart M. Sloan, to me known to be the President of UV, Inc., the general partner of UNIVERSITY VILLAGE LIMITED PARTNERSHIP, the partnership that executed the foregoing instrument, and acknowledged the said instrument to be the free and voluntary act and deed of said partnership, for the uses and purposes therein mentioned and on oath stated that he is authorized to execute the said instrument.

WITNESS my hand and official seal hereto affixed the day and year in this certificate abovewritten.

Printed Name: _____
Notary Public for the State of Washington,
residing at _____

My appointment expires: _____

CORPORATE ACKNOWLEDGMENT

STATE OF)
) ss.
COUNTY OF)

On this day of , 2003, before me, the undersigned, a Notary Public in and for said State, personally appeared and , known or identified to me to be the and of , the corporation that executed the within instrument, or the persons who executed the instrument on behalf of said corporation, and acknowledged to me that such corporation executed the same.

IN WITNESS WHEREOF, I have hereto set my hand and affixed my official seal the day and year in this certificate first above written.

Printed Name: _____
Notary Public for the state of _____
residing at _____

My appointment expires: _____

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INDIVIDUAL ACKNOWLEDGMENT

STATE OF)
) ss.
COUNTY OF)

On this day of , 20 , before me, the undersigned, a Notary Public in and for said State, personally appeared , who acknowledged that authorized to sign the foregoing instrument, and that the same is free act and deed.

IN WITNESS WHEREOF, I have hereto set my hand and affixed my official seal the day and year in this certificate first above written.

Printed Name: _____
Notary Public for the state of _____

residing at _____

My appointment expires: _____

PARTNERSHIP ACKNOWLEDGMENT

STATE OF _____)
) ss.
COUNTY OF _____)

On this _____ day of _____, 20____ before me, the undersigned, a Notary Public in and for the state of _____, duly commissioned and sworn personally appeared _____ to me known to be the _____ of _____ the partnership that executed the foregoing instrument, and acknowledged the said instrument to be the free and voluntary act and deed of said partnership, for the uses and purposes therein mentioned and on oath stated that he/she is authorized to execute the said instrument.

WITNESS my hand and official seal hereto-affixed the day and year in this certificate above written.

Printed Name: _____
Notary Public for the state of _____
residing at _____

My appointment expires: _____

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LIMITED LIABILITY COMPANY ACKNOWLEDGMENT

STATE OF _____)
) ss.
COUNTY OF _____)

On this _____ day of _____, 20____ before me, the undersigned, a Notary Public in and for the state of _____, duly commissioned and sworn personally appeared _____ to me known to be the _____ of _____ the limited liability company that executed the foregoing instrument, and acknowledged the said instrument to be the free and voluntary act and deed of said limited liability company, for the uses and purposes therein mentioned and on oath stated that he/she is authorized to execute the said instrument.

WITNESS my hand and official seal hereto-affixed the day and year in this certificate above written.

Printed Name: _____
Notary Public for the state of _____
residing at _____

My appointment expires: _____

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GUARANTY OF LEASE

THIS GUARANTY OF LEASE is made as of the 7th day of November, 2003 by J. CREW GROUP, INC., a New York corporation, with offices at 770 Broadway, New York, NY 10003 ("Guarantor").

UNIVERSITY VILLAGE LIMITED PARTNERSHIIP, a Washington limited partnership ("Landlord"), and GRACE HOLMES, INC., a Delaware corporation ("Tenant"), are entering into a certain Shopping Center Lease as of the date hereof (the "Lease"), with respect to certain premises containing approximately 7,400 square feet (the "Premises") within the shopping center located in Seattle, Washington, known as University Village.

In order to induce Landlord to lease the Premises to Tenant, Guarantor agreed to guarantee the performance of all of the terms, conditions, covenants, obligations, liabilities and agreements contained in the Lease which are required to be fulfilled or performed by Tenant, subject to the terms and provisions hereof.

1. (a) Guarantor unconditionally guarantees to Landlord and the successors and assigns of Landlord the full and punctual performance and observance by Tenant of all the terms, covenants and conditions in the Lease contained on Tenant's part to be kept, performed or observed.

(b) If at any time default shall be made by Tenant in the performance or observance of any of the terms, covenants or conditions in the Lease contained on Tenant's part to be kept, performed or observed, Guarantor will keep, perform and observe the same, as the case may be, in place and stead of Tenant.

2. Any act of Landlord, or the successors or assigns of Landlord, consisting of a waiver of any of the terms or conditions of the Lease, or the giving of any consent to any manner or thing relating to the Lease, or the granting of any indulgences or extensions of time to Tenant, may be done without

notice to Guarantor and without releasing the obligations of Guarantor hereunder. Landlord agrees to give to Guarantor notice of any Tenant default under the Lease at the address of Guarantor set forth below (or any subsequent address of which Guarantor gives Landlord written notice) in the same manner as notice to Tenant as provided under the Lease and shall afford Guarantor the period of time to cure such default as provided Tenant under the Lease with respect to such default. Failure to give any such notice by Landlord hereunder shall not discharge Guarantor of any obligation or liability under this Guaranty except that Landlord must give such notice and opportunity to cure to Guarantor prior to enforcement of any rights, remedies, liabilities or obligations under this Guaranty.

3. The obligations of Guarantor hereunder shall not be released by Landlord’s receipt, application or release of security given for the performance and observance of covenants and conditions in the Lease contained on Tenant’s part to be performed or observed; nor by any modification of the Lease, but in case of any such modification the liability of Guarantor shall be

deemed modified in accordance with the terms of any such modification of the Lease.

4. The liability of Guarantor hereunder shall in no way be affected by (a) the release or discharge of Tenant in any creditors’, receivership, bankruptcy or other proceedings; (b) the impairment, limitation or modification of the liability of the Tenant or the estate of the Tenant in bankruptcy, or of any remedy for the enforcement of Tenant’s liability under the Lease resulting from the operation of any present or future provision of the National Bankruptcy Act or other statute or from the decision in any court; (c) the rejection or disaffirmance of the Lease in any such proceedings; (d) the assignment or transfer of the Lease by Tenant or the sublease of all or any part of the premises described therein; or (e) any disability of Tenant. Guarantor further agrees that this Guaranty shall continue to be effective or be reinstated as the case may be if at any time payment, or any part thereof, of any amount pursuant to the Lease is rescinded or must otherwise be restored by Landlord as a result of the bankruptcy or reorganization of Tenant.

5. The liability of Guarantor under this Guaranty shall be continuing and shall remain in full force and effect as long as Tenant is or may be obligated to Landlord on account of any obligation covered by this Guaranty. The obligations of Guarantor to Landlord hereunder are independent of Tenant’s obligations and a separate action or actions may be brought and prosecuted by Landlord against Guarantor whether or not such action or actions are also brought against Tenant. This Guaranty constitutes a guarantee of payment when due and not of collection. Guarantor waives and agrees not to assert or otherwise take advantage of any right which it may have (a) to require Landlord to proceed against Tenant or any other person, firm or corporation or to proceed against or exhaust any security held by it at any time or to pursue any other remedy; or (b) any defense which it may have by reason of incapacity, lack of authority or other approvals relating either to Tenant or Guarantor, or based upon any statute of limitations or an election of remedies by Landlord.

6. This Guaranty shall be construed and performed in accordance with the laws of the State of Washington. Guarantor hereby irrevocably submit to the jurisdiction of King County Superior Court in Seattle, King County, Washington in any action or proceeding brought to enforce or otherwise arising out of or relating to this Guaranty and waive to the fullest extent permitted by law any objection which it may have now or hereafter to such venue or any claim that such forum is an inconvenient forum.

7. This guarantee shall apply to the Lease, any extension or renewal thereof pursuant to the exercise by Tenant of any option to extend contained in the Lease or otherwise consented to by Guarantor, and to any holdover term following the term granted by the Lease or any extension or renewal thereof.

8. This instrument may not be changed, modified, discharged or terminated orally or in any manner other than by an agreement in writing signed by Guarantor and the Landlord. If there is more than one Guarantor, the obligations of the undersigned shall be joint and several. This Guarantee shall be binding upon Guarantor and its/their successors and assigns.

9. Notwithstanding anything herein to the contrary, the obligations of Guarantor

hereunder shall not include any increased obligations of Tenant evidenced by any amendment or modification of the Lease entered into by Landlord and any successor to Tenant who is not affiliated with Guarantor.

DATED as of the day and year first above written.

GUARANTOR:

J. CREW GROUP, INC.

By: /s/ Nicholas Lamberti
Name: Nicholas Lamberti
Title: VP Controller

The Board of Directors
J. Crew Group, Inc.:

We consent to the incorporation by reference in the previously filed registration statement No. 333-60658 on Form S-8 of J. Crew Group, Inc. 1997 Stock Option Plan of our report dated April 4, 2005, with respect to the consolidated balance sheets of J. Crew Group, Inc. and subsidiaries as of January 29, 2005 and January 31, 2004, and the related consolidated statements of operations, cash flows, and changes in stockholders' deficit for each of the years in the three-year period ended January 29, 2005, and the related financial statement schedule, which report appears in the January 29, 2005 annual report on Form 10-K of J. Crew Group, Inc.

Our report refers to the adoption of Statement of Financial Accounting Standard No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" in the third quarter of fiscal 2003.

Our report also indicates that J. Crew Group, Inc. and subsidiaries have restated the consolidated statements of cash flows for each of the years in the two-year period ended January 31, 2004, to reclassify the proceeds from construction allowances from cash flows from investing activities to cash flows from operating activities.

New York, New York
April 29, 2005

**CERTIFICATION PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Millard S. Drexler, certify that:

1. I have reviewed this Annual Report on Form 10-K of J. Crew Group, Inc. and J. Crew Operating Corp.;
2. Based on my knowledge, this report 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 report;
3. Based on my knowledge, the financial statements and other financial information included in this report fairly present in all material respects the financial condition, results of operations and cash flows of each registrant as of, and for, the periods presented in this report;
4. Each registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for such registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to such registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Evaluated the effectiveness of such registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c) Disclosed in this report any change in such registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, such registrant's internal control over financial reporting; and
5. Each registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to such registrant's auditors and the audit committee of such registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect such registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in such registrant's internal control over financial reporting.

Dated: April 29, 2005

/s/ MILLARD S. DREXLER

Millard S. Drexler
Chief Executive Officer

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[EXHIBIT 31.1](#)

[CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002](#)

**CERTIFICATION PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Amanda J. Bokman, certify that:

1. I have reviewed this Annual Report on Form 10-K of J. Crew Group, Inc. and J. Crew Operating Corp.;
2. Based on my knowledge, this report 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 report;
3. Based on my knowledge, the financial statements and other financial information included in this report fairly present in all material respects the financial condition, results of operations and cash flows of each registrant as of, and for, the periods presented in this report;
4. Each registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for such registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to such registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Evaluated the effectiveness of such registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c) Disclosed in this report any change in such registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal year in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, such registrant's internal control over financial reporting; and
5. Each registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to such registrant's auditors and the audit committee of such registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect such registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in such registrant's internal control over financial reporting.

Dated: April 29, 2005

/s/ AMANDA J. BOKMAN

Amanda J. Bokman
Executive Vice-President and
Chief Financial Officer

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[EXHIBIT 31.2](#)

[CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002](#)

**CERTIFICATION PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of J.Crew Group, Inc. and J.Crew Operating Corp. (collectively, the "Company") on Form 10-K for the period ended January 29, 2005 (the "Report") as filed with the Securities and Exchange Commission, Millard S. Drexler, Chief Executive Officer of the Company, and Amanda J. Bokman, Executive Vice-President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of their knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: April 29, 2005

/s/ MILLARD S. DREXLER

Millard S. Drexler
Chief Executive Officer

/s/ AMANDA J. BOKMAN

Amanda J. Bokman
Executive Vice-President and
Chief Financial Officer

The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350) and is not being filed as part of the Report or as a separate disclosure document.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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[EXHIBIT 32.1](#)

[CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002](#)