

FOOTSTAR INC  
Form 10-K  
March 09, 2009

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**SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-K**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**  
**For the fiscal year ended January 3, 2009**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**  
**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**  
**Commission File Number 1-11681**  
**FOOTSTAR, INC.**  
(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**22-3439443**  
(I.R.S. Employer Identification No.)

**933 MacArthur Blvd., Mahwah, New Jersey**  
(Address of principal executive offices)

**07430**  
(Zip Code)

Registrant's telephone number, including area code: **(201) 934-2000**

**Securities registered pursuant to Section 12(b) of the Act:**  
None

**Securities registered pursuant to Section 12(g) of the Act:**  
Common Stock (par value \$.01 per share)  
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
 Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  Yes  No

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

Indicate by check mark 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 registrant's knowledge, in the definitive proxy statement incorporated by reference in Part III of this Form 10-K, or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

For the purpose of reporting the following market value of the registrant's common stock held by non-affiliates, the common stock held by the directors and executive officers of the registrant have been excluded. The aggregate market

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value of common stock held by non-affiliates of the registrant as of June 30, 2008, was approximately \$80.8 million based on the closing price on June 30, 2008 of \$4.08 per share.

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.  Yes  No

Number of shares outstanding of common stock, par value \$.01 per share, as of March 2, 2009: 21,524,831.

Documents Incorporated by Reference

Information required by Part III that is not provided in this report will be in either Footstar, Inc.'s Proxy Statement for the 2009 Annual Meeting of Shareholders or an amendment to this report, one of which will be filed with the Securities and Exchange Commission within 120 days after the end of the registrant's fiscal year, and is incorporated herein by reference.

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**FOOTSTAR, INC.**  
**ANNUAL REPORT ON FORM 10-K**  
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**PART I**

**INTRODUCTORY NOTE**

Footstar, Inc., which may be referred to as Footstar, the Company, we, or our is filing this Annual Report on Form 10-K for its fiscal year ended January 3, 2009.

The Company is a holding company, incorporated under the laws of the State of Delaware in 1996 and operated its businesses through its subsidiaries primarily as a retailer selling family footwear through licensed footwear departments in discount chains and wholesale arrangements since 1961.

Commencing March 2, 2004, Footstar and most of its subsidiaries filed voluntary petitions for reorganization under Chapter 11 of Title 11 of the United States Code ( Bankruptcy Code or Chapter 11 ) in the United States Bankruptcy Court ( Court ).

On February 7, 2006, the Company successfully emerged from bankruptcy and paid substantially all our creditors in full with interest. Pursuant to the guidance provided by the American Institute of Certified Public Accountants Statement of Position 90-7, Financial Reporting by Entities in Reorganization Under the Bankruptcy Code ( SOP 90-7 ), the Company has not adopted fresh-start reporting because there was no change to the holders of existing voting shares and the reorganization value of the Company's assets was greater than its post petition liabilities and allowed claims.

Until December 31, 2008, the Company had operated licensed footwear departments in discount chains since 1961, and was the only major operator of licensed footwear departments in the United States. The Company had operated licensed footwear departments in various Kmart Corporation ( Kmart ) stores. The Company also had supplied certain retail stores, including Rite Aid Corporation ( Rite Aid ), with family footwear on a wholesale basis.

As of January 3, 2009, the Company no longer operates licensed footwear departments in Kmart stores and in Rite Aid stores.

As part of its emergence from bankruptcy in February 2006, substantially all of the Company's business operations consisted of running licensed footwear departments in Kmart stores pursuant to that certain Amended and Restated Master Agreement dated as of August 24, 2005 by and between Kmart, Sears Holding Corporation ( Sears ) and the Company (the Kmart Master Agreement ), as amended by that certain Master Agreement Amendment, dated as of April 3, 2008, by and among the Company, Kmart, certain affiliates of Kmart and Sears (the Kmart Master Agreement Amendment and, collectively with the Kmart Master Agreement, the Kmart Agreement ). The Kmart Agreement expired by its terms on December 31, 2008.

In 2008, Kmart and the Company entered into discussions with respect to the rights and responsibilities of the respective parties upon termination of the Kmart Agreement as well as the sale of certain intellectual property to Kmart. As a result of such discussions, the Kmart Master Agreement Amendment was entered into on April 3, 2008, pursuant to which the Company sold such intellectual property to Kmart affiliates for approximately \$13.0 million, and reached an agreement on how the value of the inventory would be determined when sold to Kmart upon termination of the Kmart Agreement at the end of 2008 (the Kmart Settlement ).

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In May 2008, the Board of Directors determined that it was in the best interests of the Company and its stockholders to liquidate and ultimately dissolve after the expiration of the Kmart Agreement in December 2008 (and other miscellaneous contracts through the end of such term) and to sell and/or dispose of any of the Company's other remaining assets, including its Mahwah headquarters. In May 2008, the Board of Directors approved a Plan of Complete Liquidation of Footstar, Inc. (the "Original Plan"), which provides for the complete liquidation and ultimate dissolution of the Company after the expiration of the Kmart Agreement on December 31, 2008. Under the terms of the Kmart Agreement, Kmart was required to purchase from the Company all of the remaining inventory in the Kmart footwear departments at values set forth in the Kmart Agreement. The process of selling the inventory to Kmart commenced immediately after expiration of the Kmart Agreement on December 31, 2008. During 2009, the Company received \$52.8 million related to the liquidation sale of inventory from Kmart; however, the Company is currently pursuing the collection of certain additional disputed amounts for which there can be no assurance that any additional cash will be received.

Since the Company's emergency from bankruptcy on February 7, 2007, the Board of Directors has declared special cash distributions totaling \$7.00 per common share. Specifically, the Board of Directors has declared special cash distributions to shareholders in the following amounts and on the following dates: \$5.00 per common share on March 27, 2007; \$1.00 per common share on May 9, 2008; and \$1.00 per common share on January 8, 2009. In addition, the Company anticipates that if the Plan and Dissolution are approved by shareholders, then the Board of Directors will declare a special cash distribution to shareholders in the amount of \$1.90 per common share to be paid as soon as practicable following shareholder approval of the Plan and Dissolution.

The Amended Plan of Complete Dissolution and Liquidation of Footstar, Inc. (the "Plan") reflects technical and legal changes to the Original Plan consistent with Delaware corporate law and is intended to modify, supersede and replace the Original Plan in order to more efficiently facilitate the liquidation and dissolution of the Company in the best interests of shareholders. The Plan was approved by the Board of Directors on March 5, 2009.

The Plan provides for the complete, voluntary liquidation of the Company by providing for the sale of its remaining assets and the wind-down of the Company's business as described in the Plan and for distributions of available cash to shareholders as determined by the Board of Directors (the "Dissolution").

See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Factors to Consider", beginning at page 31, concerning certain other matters in connection with future events, circumstances and uncertainties that may impact the Plan and the timing and amounts of any distributions made to shareholders under the Plan.

**ITEM 1. BUSINESS**

**GENERAL**

The Company sold family footwear through licensed footwear departments and wholesale arrangements.

The Company operated licensed footwear departments from 1961 through December 2008 and was the only major operator of licensed footwear departments in the United States.

The following chart represents a summary of stores in which the Company operated licensed footwear departments for fiscal 2008, 2007 and 2006:

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	<b>Beginning of Year</b>	<b>Opened</b>	<b>Closed</b>	<b>Contract Expiration</b>	<b>End of Year</b>
Fiscal 2008					
Kmart	1,388		(11)	(1,377)	
Rite Aid	859	14	(43)	(830)	
Fiscal 2007					
Kmart	1,392		(4)		1,388
Rite Aid	854	16	(11)		859
Fiscal 2006					
Kmart	1,421		(29)		1,392
Rite Aid	859	9	(14)		854

The Company's licensed footwear operation sold family footwear and lower-priced basic and seasonal footwear in Kmart and Rite Aid stores. Our net sales from Kmart and Rite-Aid for fiscal 2008 were \$564.1 million and \$13.7 million, respectively. In addition to net sales in 2008 was the liquidating sale of the remaining inventory on hand as of December 31, 2008 in Kmart of \$52.8 million, in accordance with the Amended Master Agreement, and in Rite Aid of \$1.3 million, respectively. In its licensed footwear departments, the Company generally sold a wide variety of family footwear, including men's, women's and children's dress, casual, athletic and seasonal footwear, work shoes and slippers. As of December 31, 2005, we had been supplying Thom McAn family footwear on a wholesale basis to 1,500 Wal-Mart stores in the United States and 13 stores in Puerto Rico. Beginning in January 2006, Wal-Mart stopped purchasing Thom McAn product for its stores in the United States. Beginning in April 2007, Wal-Mart no longer sourced footwear from us for Wal-Mart stores under Wal-Mart's proprietary brands, and, beginning August 2007, Wal-Mart no longer purchased Thom McAn footwear for Wal-Mart stores in Puerto Rico. Our total sales to Wal-Mart were approximately \$0 in fiscal 2008, approximately \$2.0 million in fiscal 2007 and approximately \$8.9 million in fiscal 2006.

**EMPLOYEES**

In connection with the wind-down of our business, we terminated substantially all of our employees. As of January 3, 2009, the Company had approximately 90 employees to assist in the wind-down and anticipates it will continue to reduce this number to 10 or fewer by the end of June, 2009 as it winds down.

**EXECUTIVE OFFICERS OF THE REGISTRANT**

The following information sets forth the name, age and business experience during the past five years of the current executive officers of the Company:

Jonathan M. Couchman, 39, became President and Chief Executive Officer of Footstar effective January 1, 2009. Prior to that, on December 9, 2008 Mr. Couchman became Chief Wind-Down Officer of the Company. He was appointed Chairman of the Board of Footstar on February 7, 2006. He is the Managing Member of Couchman Capital LLC, which is the investment manager of Couchman Investments LP and Couchman International Ltd., private partnerships established in

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2001. Couchman Capital LLC is also the general partner of Couchman Partners LP, a private investment partnership established in 2001. In addition, Mr. Couchman is the President of Couchman Advisors, Inc., a management advisory company. Mr. Couchman currently serves on the Board of Directors of Golf Trust Inc., a position he has held since 2007. He is a member of the CFA Institute and the New York Society of Security Analysts and holds a Bachelor of Science in Finance from the California State University at Chico.

Michael J. Lynch, age 42, has been the Chief Financial Officer Senior Vice President of Footstar since February 7, 2006. Prior to that, he served as Senior Vice President of Finance of Meldisco. Since joining the Company in August 1995, he also served as the Division Vice President Finance at both Footstar's former Athletic and Meldisco divisions.

Maureen Richards, age 52, has been the Senior Vice President, General Counsel and Corporate Secretary of Footstar since March 2001 and was an executive officer of Footstar at the time it filed for reorganization under Chapter 11 in March 2004 and prior to March 2001, was Vice President, General Counsel and Corporate Secretary of Footstar.

Craig M. Haines, age 36, has been Vice President and Controller, and Principal Accounting Officer of Footstar since March 31, 2006. Prior thereto, he was the Company's Vice President and Controller since he joined the Company in June 2005. From November 2002 through May 2005, Mr. Haines served as Executive Vice President, Finance and Administration for National Vision Administrators, LLC.

**AVAILABLE INFORMATION**

We make available free of charge through our web site, [www.footstar.com](http://www.footstar.com), all materials that we file electronically with the Securities and Exchange Commission (the Commission or the SEC), including our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports, filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act). During the period covered by this Form 10-K, we made all such materials available through our web site as soon as reasonably practicable after filing such materials with the SEC.

You may also read and copy any materials filed by us with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549, and you may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet web site, [www.sec.gov](http://www.sec.gov), which contains reports, proxy and information statements and other information which we file electronically with the SEC. A copy of Footstar's Corporate Governance Guidelines and its Code of Conduct and Compliance Program are posted on the Corporate Governance section of the Company's website, [www.footstar.com](http://www.footstar.com), and are available in print to any shareholder who requests copies by contacting Maureen Richards, Senior Vice President, General Counsel and Corporate Secretary, at the Company's principal executive office set forth above.



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**ITEM 1A. RISK FACTORS**

The matters discussed in this Annual Report on Form 10-K include forward-looking statements that involve significant risks and uncertainties and that are made in reliance upon the safe harbor provisions of Section 27A of the Securities Act and Section 21E of the Exchange Act. These statements may be identified by the use of words, such as: anticipate, estimates, should, expect, project, intend, plan, believe and other words and terms of similar connection with any discussion of our financial statements, business, results of operations, liquidity, future operating or financial performance and other future events and circumstances. These statements are neither promises nor guarantees. A number of important risks and uncertainties, including those identified below and those factors included in this Annual Report on Form 10-K under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations Factors to Consider, beginning at page 31, each of which is a risk factor and is incorporated into this Item 1A by reference and Recent Events, beginning on page 19, each of which is a risk factor and is incorporated into this Item 1A by reference, as well as risks and uncertainties discussed elsewhere in this Form 10-K, could cause our actual results to differ materially from those expressed or implied in our forward-looking statements. In addition to the above-referenced statements and factors which are set forth elsewhere in our Annual Report on Form 10-K and incorporated herein by reference, we set forth the following risks and uncertainties related to our business.

***We may not meet the anticipated timing for the Dissolution and liquidation.***

Promptly following the meeting, if our shareholders approve the Plan and our Dissolution, we intend to file a certificate of dissolution with the Secretary of State of Delaware and work toward the sale of our remaining assets and the winding up of our remaining business. The Company anticipates that if the Plan and Dissolution are approved by shareholders, then its Board of Directors will declare a special cash distribution to shareholders in the amount of \$1.90 per common share to be paid to shareholders as soon as practicable following shareholder approval of the Plan and Dissolution. After paying all of our liabilities and obligations, we plan to establish a contingency reserve to cover any unknown liabilities. We intend to begin making distributions of liquidation proceeds to our shareholders within three to six months (or sooner) from the time we file our certificate of dissolution. Thereafter, we intend to distribute remaining liquidation proceeds as promptly as practicable following the sale of our remaining assets, subject to payment or provision for the payment of operating and administrative expenses during the liquidation, known obligations and establishing a contingency reserve. There are a number of factors that could delay our anticipated timetable, including the following:

delays in the disposition of our remaining assets;

unanticipated lawsuits or other claims asserted against us;

unanticipated legal, regulatory, governmental, tax or administrative requirements; and

delays in settling our remaining obligations.

***We cannot determine with certainty the amount of distributions that will be made to our shareholders.***

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We cannot determine with precision at this time the amount of distributions to our shareholders pursuant to the Plan. This determination depends on a variety of factors, including, but not limited to, the amount required to settle known and unknown debts and liabilities, the resolution of any contingent liabilities, the amount of any necessary or appropriate contingency reserve, the net proceeds, if any, from the sale of our remaining assets, and other factors.

***Adverse U.S. economic conditions and the current turmoil in the U.S. capital and credit markets could limit demand for our property in Mahwah, New Jersey, which contains our corporate headquarters and 21 acres of land, and, thus, we may not be able to timely sell our property in Mahwah or on acceptable terms.***

The economy in the United States is currently experiencing unprecedented disruptions, including increased levels of unemployment, the failure and near failure of a number of large financial institutions, reduced liquidity and increased credit risk premiums for a number of market participants. Economic conditions may be affected by numerous factors, including inflation and employment levels, energy prices, recessionary concerns, changes in currency exchange rates, the availability of debt and interest rate fluctuations. At this time, it is unclear whether, and to what extent, the actions taken by the U.S. government, including the passage of the Emergency Stabilization Act of 2008, the Troubled Assets Relief Program, the American Recovery and Reinvestment Act of 2009 and other measures currently being implemented or contemplated will mitigate the effects of the crisis. The current turmoil in the capital and credit markets could limit demand for our property in Mahwah, New Jersey, which contains our corporate headquarters and 21 acres of land and which we have been marketing since March 2007. At this time we cannot predict the extent or duration of any negative impact that the current disruptions in the U.S. economy will have on our ability to timely sell our corporate headquarters or on acceptable terms.

***We may not be able to settle all of our obligations to creditors.***

We have current obligations to creditors. Our estimate of ultimate distributions to our shareholders takes into account all of our known obligations and our best estimate of the amount reasonably required to satisfy such obligations. As part of our dissolution process, we will attempt to settle those obligations with our creditors. We cannot assure you that we will be able to settle all of these obligations or that they can be settled for the amounts we have estimated for purposes of calculating the likely distribution to shareholders. If we are unable to reach agreement with a creditor relating to an obligation, that creditor may bring a lawsuit against us. Amounts required to settle obligations or defend lawsuits in excess of the estimated amounts will result in distributions to shareholders that are smaller than those that we presently estimate or may eliminate distributions entirely.

***We will continue to incur claims, liabilities and expenses, which will reduce the amount available for distribution to shareholders.***

We will continue to incur claims, liabilities and expenses (such as salaries and benefits, directors and officers insurance, payroll and local taxes, facilities costs, legal, accounting and consulting fees and miscellaneous office expenses) as we wind up. These expenses will reduce the amount ultimately available for distribution to our shareholders.

***We will continue to incur the expenses of complying with public company reporting requirements.***

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We currently comply with the applicable reporting requirements of the Exchange Act. In order to curtail these expenses, after filing our certificate of dissolution with the Delaware Secretary of State, we intend to deregister our common stock or seek relief from certain of our public company reporting requirements from the SEC. We anticipate that, if we are unable to deregister our securities and have to pursue SEC relief and such relief is granted by the SEC, we will continue to file current reports on Form 8-K to disclose material events relating to our liquidation, along with any other reports that the SEC may require. However, we cannot offer any assurances as to when, if ever, the SEC may grant such relief or as to the actual savings that we may realize should such relief be granted.

***Each shareholder may be liable to our creditors for an amount up to the amount distributed to such shareholder by us if our reserves for payments to creditors are inadequate.***

If our shareholders approve the Plan and our Dissolution, we expect to file a certificate of dissolution with the Secretary of State of Delaware promptly following the Meeting. Although the legal effect of the filing and effectiveness of the certificate of dissolution will be to dissolve the Company, as required by Delaware law we will continue to exist as a non-operating entity for at least three years after the Dissolution becomes effective (which we expect will be the date on which we file the certificate of dissolution with the Delaware Secretary of State) or for such longer period as the Delaware Court of Chancery directs, for the purpose of prosecuting and defending lawsuits, settling and closing our business, disposing of our property, discharging our liabilities and distributing to our shareholders any remaining assets. Under applicable Delaware law, in the event we do not resolve all claims against the Company, each of our shareholders could be held liable for payment to our creditors up to the amount distributed to such shareholder in the liquidation. In such event, a shareholder could be required to return up to all amounts received as distributions pursuant to the Plan and ultimately could receive nothing under the Plan. Moreover, even though a shareholder has paid taxes on amounts previously received, a repayment of all or a portion of such amount will not result in a recalculation of the gain or loss on the liquidation. Instead, a shareholder's repayment will generally be deductible as a capital loss in the year in which the contingent liability is paid, and such capital loss cannot be carried back to offset any liquidation gain recognized earlier. See Certain Federal Income Tax Consequences. We cannot assure you that any contingency reserve that we plan to establish will be adequate to cover all expenses and liabilities.

***Recordation of transfers of our common stock on our stock transfer books will be restricted as of the Final Record Date, and thereafter it generally will not be possible for shareholders to change record ownership of our stock.***

The Company intends to discontinue recording transfers of our common stock at the close of business on the date specified by the Board for the effectiveness of the certificate of dissolution (the Final Record Date). Thereafter, certificates representing our common stock will not be assignable or transferable on the books of the Company except by will, intestate succession or operation of law. However, until trading is halted through termination of registration of our shares of common stock, after the Final Record Date, we believe that any trades of shares of our common stock will be tracked and marked with a due bill by the Depository Trust Company.

On or after the Final Record Date, we intend to make liquidation distributions pursuant to the Plan and deregister our common stock or seek relief from the SEC of certain of our public company

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reporting requirements. The liquidation distributions under the Plan shall be in complete cancellation of all of the outstanding shares of our common stock. From and after the Final Record Date, and subject to applicable law, each holder of our common stock will have the right to receive distributions pursuant to, and in accordance with, the Plan. The proportionate interests of all of the shareholders of the Company will be fixed in the books of the Company on the basis of their respective stock holdings at the close of business on the Final Record Date. Further, after the Final Record Date, any distributions made by the Company will be made solely to the shareholders of record at the close of business on the Final Record Date, except as may be necessary to reflect subsequent transfers recorded on the books of the Company as a result of any assignments by will, intestate succession or operation of law.

***Shareholders may not be able to recognize a loss for federal income tax purposes until they receive a final distribution from us, which may be three years or more after our Dissolution.***

As a result of our liquidation, for federal income tax purposes shareholders will recognize gain or loss equal to the difference between (1) the sum of the amount of cash and the aggregate fair market value of any property distributed to them (reduced by any liability assumed or subject to which it is taken), and (2) their tax basis in their shares of our common stock. A shareholder's tax basis in our shares will depend upon various factors, including the shareholder's cost and the amount and nature of any distributions received with respect thereto. A shareholder generally may recognize a loss only when he, she or it has received a final distribution from us, which may be as much as three years (or ten years if our Board of Directors determines to liquidate our assets in accordance with Section 281(b) of the Delaware General Corporation Law) after our Dissolution. However, if we are unable to sell our Mahwah property prior to the third anniversary of the filing of the certificate of dissolution, we may transfer such property into a liquidating trust, in which event we may make a final distribution after the third anniversary of the filing of the certificate of dissolution.

***Our Board of Directors may amend, modify, abandon or delay implementation of the Plan and our Dissolution, even if approved by our shareholders.***

Even if the Plan and our Dissolution are approved by our shareholders, our Board of Directors has the right, in its discretion, to amend, modify, abandon or delay implementation of the Plan and our Dissolution to the extent permitted by the Delaware General Corporation Law, if it determines that doing so is in the best interests of the Company and our shareholders.

***We have a dispute with Kmart under the Kmart Agreement related to the sale of all our remaining inventory to Kmart and additional disputes with Kmart may arise in the future.***

Notwithstanding the Company's sale of all its remaining inventory to Kmart under the terms of the Kmart Agreement immediately following termination of the Kmart Agreement in accordance with the provisions thereof, there is an outstanding dispute with respect to the value of inventory and that we are in the process of trying to resolve and additional disputes may arise related to the Kmart Agreement.

***See Forward-Looking Statements in Item 7 for additional risk factors to consider.***

**ITEM 1 B. UNRESOLVED STAFF COMMENTS**

None.

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**ITEM 2. PROPERTIES**

As of January 3, 2009, we no longer operated licensed footwear departments.

Our corporate headquarters is located in 129,000 square feet of owned office space at our 21 acre property in Mahwah, New Jersey. In connection with the wind-down of our business, we are actively pursuing the sale of our property in Mahwah.

Our corporate tax department is located in 3,500 square feet of leased office space in Worcester, Massachusetts. The lease for this property expires at the end of April 2009 and no renewals are currently anticipated.

In connection with the Company's discontinued operations in 1995, the Company entered into two subleases of locations formerly occupied by its Thom McAn stores. One of these subleases expired on December 31, 2008 but the subtenant failed to vacate the premises and the overlandlord has commenced holdover proceedings to evict such tenant. The other lease expires effective February 1, 2014. The Company believes that there has been a novation of its obligations under such lease and may in the future bring litigation to have a court finally determine such issue.

**ITEM 3. LEGAL PROCEEDINGS**

We are involved in various claims and legal proceedings arising in the ordinary course of business. We intend to defend vigorously against such claims in all such proceedings. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources, divert management's attention from our business objectives and could adversely affect our business. We do not believe any of them will have a material adverse effect on our financial position. Estimates of the probable costs for resolution of these claims are accrued to the extent that they can be reasonably estimated. These estimates are based on an analysis of potential outcomes, assuming a combination of litigation and settlement strategies. These estimates also take into account any claim relating to events that occurred prior to our bankruptcy filing, which were required to be reported in a proof of claim filed with the Bankruptcy Court. However, legal proceedings are subject to significant uncertainties, the outcomes of which are difficult to predict, and assumptions and strategies may change. Consequently, we are unable to ascertain the ultimate financial impact of any legal proceedings.

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

None

**PART II**

**ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

After the delisting of our common stock from the NYSE on December 30, 2003, our common stock was traded on the over-the-counter bulletin board (OTCBB) under the symbol FTSTQ.PK. Effective March 13, 2006 our symbol changed to FTAR.OB. Our common stock is quoted on the OTCBB and on the Pink Sheets LLC. Prices shown below reflect the quarterly high and low bid

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quotations for the common stock as reported on the OTCBB System. The over-the-counter market quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission, may not necessarily reflect actual transactions and have not been adjusted for dividends. As of February 27, 2009, there were 1,972 shareholders of record (not including the number of persons or entities holding stock in nominee or street name through various banks and brokerage firms). Information concerning the high and low closing bid quotations of our common stock is set forth below:

	HIGH	LOW
<b>2007</b>		
First Quarter	\$ 8.50	\$ 6.10
Second Quarter	\$ 9.12	\$ 4.10
Third Quarter	\$ 4.72	\$ 4.00
Fourth Quarter	\$ 4.92	\$ 4.20

<b>2008</b>		
First Quarter	\$ 4.70	\$ 4.25
Second Quarter	\$ 5.35	\$ 4.10
Third Quarter	\$ 4.09	\$ 3.40
Fourth Quarter	\$ 3.64	\$ 2.80

Since the Company emerged from bankruptcy on February 7, 2006, the Board of Directors has declared special cash distributions totaling \$7.00 per common share.

On March 27, 2007, the Company announced that its Board of Directors declared a special cash distribution to stockholders in the amount of \$5.00 per common share. The Company recorded this distribution effective the date the declaration was made by the Board of Directors. The special cash distribution totaling \$104.8 million was paid on April 30, 2007.

On May 9, 2008, the Company announced that its Board of Directors declared a special cash distribution to stockholders in the amount of \$1.00 per common share. The Company recorded this distribution effective the date the declaration was made by the Board of Directors. The special cash distribution totaling \$21.3 million was paid on June 3, 2008.

On January 8, 2009, the Company announced that its Board of Directors declared a special cash distribution to stockholders in the amount of \$1.00 per common share. The Company recorded this distribution effective the date the declaration was made by the Board of Directors. The special cash distribution totaling \$21.5 million was paid on January 27, 2009.

On February 4, 2009, the Company entered into Amendment No. 2 ( Amendment No. 2 ) to its Rights Agreement, dated as of March 8, 1999, as amended as of May 31, 2002 (as amended, the Rights Agreement ), between it and Mellon Investor Services LLC, a New Jersey limited liability company (formerly ChaseMellon Shareholder Services, L.L.C.), as Rights Agent, pursuant to which the terms of the outstanding preferred share purchase rights were amended.

The Rights Agreement was amended by Amendment No. 2 in order to protect stockholder value by attempting to prevent a possible limitation on the Company's ability to use its U.S. net operating loss carryovers. The Company has experienced significant losses in the United States, and under the Internal Revenue Code of 1986, as amended (the Code ), and rules and regulations promulgated by the Internal Revenue Service, the Company may carry forward these losses in certain

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circumstances to offset any current and future taxable income and thus reduce federal income tax liability, subject to certain requirements and restrictions. However, if the Company experiences an ownership change as defined in Section 382 of the Code, the Company's ability to use the net operating losses could be severely limited.

After approval of the Plan and Dissolution by our shareholders and the filing of our certificate of dissolution with the Delaware Secretary of State, we plan to sell or liquidate any remaining assets and pay all of our known and undisputed liabilities and obligations. We intend to then establish a contingency reserve to cover any unknown, disputed or contingent liabilities and intend to distribute remaining amounts to shareholders as and when our Board of Directors deems appropriate. We expect that if the Plan and Dissolution are approved by shareholders, then our Board of Directors will declare a special cash distribution to shareholders in the amount of \$1.90 per common share to be paid to shareholders as promptly as practicable following shareholder approval of the Plan and Dissolution. We anticipate that we will begin making distributions of liquidation proceeds to our shareholders within three to six months (or sooner) from the time we file our certificate of dissolution, in accordance with the Plan and Delaware law. We also intend to distribute remaining liquidation proceeds as promptly as practicable following the sale or liquidation of our remaining assets, subject to payment or provisions for the payment of known obligations and establishing a contingency reserve. It is possible that unanticipated lawsuits or other claims will be asserted against us, which could result in certain distributions to our shareholders being delayed for possibly several years until the resolution of any such lawsuit or other claim.

Because of the uncertainties as to the ultimate settlement amount of our remaining liabilities and expenditures we will face during liquidation, we are not able to predict with precision or certainty specific amounts, or timing, of future liquidation distributions. We are currently evaluating the market value of our limited remaining non-cash assets. At the present time, although we are not able to predict with certainty whether sales proceeds from our remaining assets will differ materially from amounts recorded for those assets on our balance sheet at January 3, 2009, we currently estimate that the amount ultimately distributed to our shareholders will be between \$2.65 and \$3.45 per common share, including the special cash distribution to shareholders in the amount of \$1.90 per common share that we anticipate will be declared by the Board of Directors if the Plan and Dissolution are approved by shareholders. To the extent that the value of our assets is less, or the amount of our liabilities or the amounts that we expend during liquidation are greater, than we anticipate, our shareholders could receive less than we currently estimate.

Please refer to Introductory Note and Item 1A, Risk Factors, above, in connection with the wind-down of the Company's businesses in connection with the termination of the Kmart Agreement.

**Stock Performance Graph**

The graph set forth below shows the cumulative total return to stockholders over the five-year fiscal period ended January 2, 2009, assuming an investment of \$100 on January 2, 2004 in each of Footstar's common stock, the NASDAQ Composite Index and the S&P Footwear Index. The graph assumes all dividends have been reinvested. The stock price performance included in the graph is not necessarily indicative of future stock price performance.

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**COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\***  
Among Footstar, Inc., The NASDAQ Composite Index  
And The S&P Footwear Index

\* \$100 invested on 1/2/04 in stock & index-including reinvestment of dividends.

Fiscal year ending January 2.

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The Performance Graph in this Item 5 is not deemed to be soliciting material or to be filed with the SEC or subject to Regulation 14A or 14C under the Exchange Act or to the liabilities of Section 18 of the Exchange Act, and will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended (the Securities Act ) or the Exchange Act, except to the extent we specifically incorporate it by reference into such a filing.

**Recent Sales of Unregistered Securities**

We did not make any unregistered sales of our common stock during the 2008 fiscal year.

**Issuer Purchases of Equity Securities**

We did not repurchase any shares of our common stock during the three months ended January 3, 2009.



**Table of Contents****ITEM 6. SELECTED FINANCIAL DATA  
FIVE-YEAR HISTORICAL FINANCIAL SUMMARY**

The following selected consolidated financial data presented below are derived from the Consolidated Financial Statements and related Notes of the Company, and should be read in connection with those statements, some of which are included herein. The information set forth below is not necessarily indicative of future results and should be read in conjunction with Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations*.

<i>(dollars in millions except per share data)</i>	<b>2008</b>	2007	2006	2005	2004
Revenue:					
Net sales	<b>\$ 580.0</b>	\$ 637.0	\$ 666.7	\$ 715.4	\$ 800.2
Liquidation of inventory	<b>54.2</b>				
Total revenue	<b>634.2</b>	637.0	666.7	715.4	800.2
Cost:					
Cost of sales	<b>396.7</b>	427.4	452.1	490.4	535.8
Cost of liquidation of inventory	<b>59.1</b>				
<b>Total cost</b>	<b>455.8</b>	427.4	452.1	490.4	535.8
Total gross profit	<b>178.4</b>	209.6	214.6	225.0	264.4
Store operating, selling, general and administrative expenses	<b>146.8</b>	148.6	160.6	183.1	236.1
Depreciation and amortization	<b>4.5</b>	8.1	8.8	7.7	21.7
Loss on impairment of long-lived assets	<b>10.8</b>				
Gain on cancellation of retiree benefit plan	<b>(22.3)</b>				
Gain on sale of intangible assets	<b>(10.5)</b>				
(Gain) loss on Kmart Agreement <sup>(1)</sup>	<b>(5.0)</b>				6.3
Other income		(0.6)			(9.2)
Interest expense	<b>1.1</b>	1.2	1.6	4.6	11.0
Interest income	<b>(0.7)</b>	(2.6)	(3.8)		
<b>Income (loss) before reorganization items, income taxes, minority interests and discontinued operations</b>	<b>53.7</b>	54.9	47.4	29.6	(1.5)
Reorganization items <sup>(2)</sup>				(14.6)	(37.1)
<b>Income (loss) before income taxes, minority interests and discontinued operations</b>	<b>53.7</b>	54.9	47.4	15.0	(38.6)
(Provision) benefit for income taxes <sup>(3)</sup>	<b>(1.3)</b>	(2.1)	(1.4)	(4.2)	2.9
<b>Income (loss) before minority interests and discontinued operations</b>	<b>52.4</b>	52.8	46.0	10.8	(35.7)
Minority interests in loss					11.0
<b>Income (loss) from continuing operations</b>	<b>52.4</b>	52.8	46.0	10.8	(24.7)
Income (loss) from discontinued operations, net of tax <sup>(4)</sup>	<b>1.3</b>	(0.8)	(0.8)	4.7	(66.7)

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Gain from disposal of discontinued operations, net of tax			0.1	8.9	21.4
<b>Net income (loss)</b>	<b>\$ 53.7</b>	\$ 52.0	\$ 45.3	\$ 24.4	\$ (70.0)
<b>Basic income (loss) per share from continuing operations</b>	<b>\$ 2.51</b>	\$ 2.56	\$ 2.23	\$ 0.53	\$ (1.20)
<b>Diluted income (loss) per share from continuing operations</b>	<b>\$ 2.48</b>	\$ 2.52	\$ 2.21	\$ 0.53	\$ (1.20)
Special distribution declared per common share	<b>\$ 1.00</b>	\$ 5.00			
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**Table of Contents****ITEM 6. SELECTED FINANCIAL DATA, cont.  
FIVE-YEAR HISTORICAL FINANCIAL SUMMARY**

<i>(dollars in millions)</i>	<b>2008</b>	2007	2006	2005	2004
<b>Balance Sheet Data</b>					
Current assets:					
Cash and cash equivalents	\$ <b>56.6</b>	\$ 53.8	\$ 101.3	\$ 196.1	\$ 189.6
Inventories		86.7	92.0	89.2	98.9
Receivables and other	<b>65.1</b>	15.8	18.5	30.3	50.5
Assets held for sale	<b>6.2</b>				
Assets related to discontinued operations				0.1	6.2
Total current assets	<b>127.9</b>	156.3	211.8	315.7	345.2
Property and equipment, net		20.7	25.2	28.9	35.4
Other assets	<b>1.0</b>	4.6	8.3	12.1	13.5
Total assets	<b>\$ 128.9</b>	\$ 181.6	\$ 245.3	\$ 356.7	\$ 394.1
Current liabilities:					
Amount due under Kmart Settlement <sup>(1)</sup>	\$	\$ 5.1	\$	\$	\$ 45.0
Other current liabilities	<b>20.7</b>	69.9	78.5	107.8	98.0
Liability held for sale	<b>2.0</b>				
Liabilities related to discontinued operations	<b>0.5</b>	0.9	2.3	7.4	3.5
Liabilities subject to compromise		0.5	1.2	125.5	152.3
Total current liabilities	<b>23.2</b>	76.4	82.0	240.7	298.8
Other long term liabilities	<b>1.2</b>	26.1	26.6	35.0	38.5
Amount due under Kmart Settlement <sup>(1)</sup>			5.2	5.5	5.5
Total liabilities	<b>24.4</b>	102.5	113.8	281.2	342.8
Shareholders' equity	<b>104.5</b>	79.1	131.5	75.5	51.3
Total liabilities and shareholders equity	<b>\$ 128.9</b>	\$ 181.6	\$ 245.3	\$ 356.7	\$ 394.1

<sup>(1)</sup> Represents additional charge incurred on Kmart Settlement and the elimination of the minority interests as part of the cure payment and amount due relating to

future store  
closings for  
fiscal 2004 and  
2007. Upon the  
expiration of the  
Kmart  
Agreement all  
claims not yet  
due or payable  
relating to  
future store  
closin