Hyatt Hotels Corp
Form 4
March 17, 2016

FORM 4

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

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

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL
OMB Number: 3235-0287
Expires: January 31, 2005
Estimated average burden hours per response... 0.5

(Print or Type Responses)

1. Name and Address of Reporting Person *
GS SUNRAY HOLDINGS SUBCO I, L.L.C.
(Last) (First) (Middle)
200 WEST STREET
(Street)
NEW YORK, NY 10282
(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
Hyatt Hotels Corp [H]

3. Date of Earliest Transaction (Month/Day/Year)
03/15-04:00/2016

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer
(Check all applicable)
_____ Director _____ 10% Owner
_____ Officer (give title below) _____ Other (specify below)

6. Individual or Joint/Group Filing(Check Applicable Line)
___ Form filed by One Reporting Person
_X_ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Class A Common Stock	03/15-04:00/2016		A		393	A	$ 0	97,059	I	See footnotes (1) (2) (3) (4) (5)

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.

SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and A Underlying S (Instr. 3 and
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title
Restricted Stock Units	$ 0							03/31-04:00/2016	03/31-04:00/2016	Class A Common Stock
Class B Common Stock	$ 0							(7)	(7)	Class A Common Stock

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
GS SUNRAY HOLDINGS SUBCO I, L.L.C. 200 WEST STREET NEW YORK, NY 10282				
GS SUNRAY HOLDINGS SUBCO II, L.L.C. 200 WEST STREET NEW YORK, NY 10282				
GS SUNRAY HOLDINGS PARALLEL SUBCO, L.L.C. 200 WEST STREET NEW YORK, NY 10282				

Signatures

/s/ Yvette Kosic, Attorney-in-fact	03/17-04:00/2016
**Signature of Reporting Person	Date
/s/ Yvette Kosic, Attorney-in-fact	03/17-04:00/2016
**Signature of Reporting Person	Date
/s/ Yvette Kosic, Attorney-in-fact	03/17-04:00/2016
**Signature of Reporting Person	Date

Explanation of Responses:

*	If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).
**	Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
(1)	This statement is being filed by The Goldman Sachs Group, Inc. ("GS Group"), Goldman, Sachs & Co. ("Goldman Sachs"), GS Capital Partners VI Fund, L.P. ("GS Capital"), GS Capital Partners VI Offshore Fund, L.P. ("GS Offshore"), GS Capital Partners VI Parallel, L.P. ("GS Parallel"), GS Capital Partners VI GmbH & Co. KG ("GS Germany", and together with GS Capital, GS Offshore and GS Parallel, the "Limited Partnerships"), GS Sunray Holdings Subco I, L.L.C. ("GS Sunray I"), GS Sunray Holdings Subco II, L.L.C. ("GS Sunray II"), GS Sunray Holdings Parallel Subco, L.L.C. ("GS Sunray Parallel", and together with GS Sunray I and GS Sunray II, the "Sunray Entities"), GSCP VI Advisors, L.L.C. ("GSCP Advisors"), GSCP VI Offshore Advisors, L.L.C. ("GSCP Offshore Advisors"), (continued in next footnote)
(2)	GS Advisors VI, L.L.C. ("GS Advisors") and Goldman, Sachs Management GP GmbH ("GS GmbH", and together with GSCP Advisors, GSCP Offshore Advisors, GS Advisors, the Limited Partnerships, the Sunray Entities, Goldman Sachs and GS Group, the "Reporting Persons"). Goldman Sachs is a wholly-owned subsidiary of GS Group. Goldman Sachs is the investment manager for certain of the Limited Partnerships. The Sunray Entities are owned directly and indirectly by the Limited Partnerships, of which affiliates of Goldman Sachs and GS Group are the general partner, managing limited partner or managing partner.
(3)	Due to the electronic system's limitation of 10 Reporting Persons per joint filing, this statement is being filed in duplicate.
(4)	On March 15, 2016, 393 shares of Class A Common Stock were granted to Richard A. Friedman, a managing director of Goldman Sachs, in his capacity as a director of Hyatt Hotels Corporation (the "Company") pursuant to the Third Amended and Restated Hyatt Hotels Corporation Long-Term Incentive Plan under the Hyatt Hotels Corporation Non-Employee Director Compensation Program (the "Plan"). Mr. Friedman has an understanding with GS Group pursuant to which such shares are held for the benefit of GS Group.
(5)	GS Group may be deemed to beneficially own 22,908 shares of Class A Common Stock that were granted to Richard A. Friedman in his capacity as a director of the Company pursuant to the Plan. Mr. Friedman has an understanding with GS Group pursuant to which such shares are held for the benefit of GS Group. GS Group beneficially owns directly 7,096 shares of Class A Common Stock. Goldman Sachs beneficially owns directly and GS Group may be deemed to beneficially own indirectly 67,055 shares of Class A Common Stock and Goldman Sachs also had open short positions of 29,326 shares of Class A Common Stock, reflecting changes due to exempt transactions.
(6)	GS Group may be deemed to beneficially own an aggregate of 3,068 restricted stock units that were granted to Richard A. Friedman in his capacity as a director of the Company. Mr. Friedman has an understanding with GS Group pursuant to which such restricted stock units are held for the benefit of GS Group. Each restricted stock unit represents the contingent right to receive one share of Class A Common Stock and is fully vested.
(7)	Each share of Class B Common Stock is convertible at any time, at the option of the holder, into one share of Class A Common Stock. In addition, each share of Class B Common Stock will convert automatically into one share of Class A Common Stock upon any transfer, except for certain permitted transfers as described in the Company's Amended and Restated Certificate of Incorporation. Goldman Sachs and GS Group may each be deemed to beneficially own indirectly 12,654,050 shares of the Company's Class A Common Stock by reason of the direct beneficial ownership of 12,654,050 shares of the Company's Class B Common Stock, in the aggregate, by the Sunray Entities. Each Reporting Person disclaims beneficial ownership of the securities reported herein except to the extent of its pecuniary interest therein.
(8)	GS Sunray I may be deemed to beneficially own 5,514,889 shares of Class A Common Stock by reason of its direct beneficial ownership of 5,514,889 shares of Class B Common Stock. GS Sunray II may be deemed to beneficially own 5,514,889 shares of Class A Common Stock by reason of its direct beneficial ownership of 5,514,889 shares of Class B Common Stock. GS Sunray Parallel may be deemed to beneficially own 1,624,272 shares of Class A Common Stock by reason of its direct beneficial ownership of 1,624,272 shares of Class B Common Stock.
(9)	GS Capital, and its general partner GSCP Advisors, may be deemed to beneficially own indirectly 5,906,782 shares of Class A Common Stock by reason of the direct beneficial ownership of Class B Common Stock by GS Sunray I and GS Sunray II. GS Offshore, and its general partner GSCP Offshore Advisors, may be deemed to beneficially own indirectly 4,913,071 shares of Class A Common Stock by reason of the direct beneficial ownership of Class B Common Stock by GS Sunray I and GS Sunray II. GS Parallel, and its general partner GS Advisors, may be deemed to beneficially own indirectly 1,624,272 shares of Class A Common Stock by reason of the direct beneficial ownership of Class B Common Stock by GS Sunray Parallel. GS Germany, and its general partner, GS GmbH, may be deemed to beneficially own indirectly 209,925 shares of Class A Common Stock by reason of the direct beneficial ownership of Class B Common Stock by GS Sunray I and GS Sunray II.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. /TD> 3,116

Net income

2,870,136 54,315 2,924,451

Accretion of Trust Fund relating to Common Stock subject to possible conversion

(793,712) (23,628) (817,340)

Net income available to common stockholders

$2,076,424 $30,687 $2,107,111

Weighted average shares outstanding

16,668,534 4,670,245

Basic and diluted net income per share

$0.12 $0.01

Endeavor was formed on July 22, 2005 to serve as a vehicle to effect a merger, capital stock exchange, asset acquisition or other similar business combination with an operating business. We intend to utilize cash derived from the proceeds of our recently completed public offering, our capital stock, debt or a combination of cash, capital stock and debt, in effecting a business combination.

Endeavor consummated our initial public offering on December 21, 2005. All activity from July 22, 2005 through December 21, 2005 related to our formation and our initial public offering. Since December 21, 2005, we have been searching for prospective target businesses to acquire.

Endeavor had net income of $2,870,136 for the year ended December 31, 2006 consisting of $3,974,013 of dividend income, $1,101,412 of general, selling and administrative expenses, and $2,465 of income tax expense.

Endeavor had net income of $2,924,451 for the period July 22, 2005 (inception) to December 31, 2006 consisting of $4,092,212 of dividend income, $1,164,645 of general, selling and administrative expenses and $3,116 of income tax expense.

Endeavor had net income of $54,315 for the fiscal period July 22, 2005 (inception) to December 31, 2005.

Upon consummation of Endeavor s initial public offering (Offering), $121,030,234 of the net proceeds was deposited in trust, with the remaining net proceeds of $1,316,746 becoming available to pay for business, legal and accounting due diligence on prospective acquisitions and continuing general and administrative expenses. We have used substantially all of the net proceeds of our initial public offering not held in trust to identify and evaluate prospective acquisition candidates, select the target business, and structure, negotiate and consummate the business combination. We intend to utilize our cash, including the funds held in the trust fund, capital stock, debt or a combination of the foregoing to effect a business combination. To the extent that our capital stock or debt securities are used in whole or in part as consideration to effect a business combination, the proceeds held in the trust fund as well as any other available cash will be used to finance the operations of the target business. At December 31, 2006, we had current assets (excluding cash held in the trust fund) of $283,265 and current liabilities of $260,076, leaving us with working capital of $23,189, net of $125,113,007 which is cash held in trust. Our officers have agreed to advance us enough capital in order to consummate the acquisition of American Apparel described below.

136

Table of Contents

The Use of Proceeds section of Endeavor s prospectus in connection with its IPO provided the estimate and projected allocation of how the $1,385,000 held outside of the trust would be used in connection with Endeavor s search for a potential business combination target and operations and Exchange Act reporting prior to the consummation of a business combination. This estimate included approximately $180,000 payable for office space and administrative fees, $300,000 for due diligence of prospective target businesses, $300,000 related to the expense of a business combination and $80,000 for legal and accounting expenses related to Exchange Act reporting. As a result of the large number of target businesses examined by Endeavor and the amount of time that elapsed prior to targeting and entering into a definitive Acquisition Agreement with American Apparel, Endeavor expects that some of these estimates will be exceeded. Additionally, legal and accounting expenses related to Exchange Act reporting through December 31, 2006 of $156,650 were higher than projected.

Endeavor s Certificate of Incorporation provides for Endeavor s mandatory liquidation in the event that it does not consummate a business combination within 18 months from the date of the consummation of the Offering (July 21, 2007), or 24 months from the consummation of the Offering (December 21, 2007) if certain extension criteria have been satisfied. In the event of liquidation, it is likely that the per share value of the residual assets remaining available for distribution (including Trust Account assets) will be less than the Offering price per share in the Offering due to costs related to the Offering and since no value would be attributed to the warrants contained in the units sold. Messrs. Watson and Ledecky will be personally liable under certain circumstances (for example, if a vendor successfully makes a claim against funds in the trust account) to ensure that the proceeds in the trust account are not further reduced by the claims of prospective target businesses and vendors or other entities that are owed money by Endeavor for services rendered or products sold to Endeavor. As of December 31, 2006, the estimated value of Mr. Watson s and Mr. Ledecky s obligation is $25,639, based on cash held outside the trust account of approximately $400,910 and approximately $426,539 owed to parties who have not waived claims against the trust account.

The mandatory liquidation described above raises substantial doubt about the Endeavor s ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Endeavor is obligated to pay to Ironbound Partners a monthly fee of $7,500 for general and administrative services.

On December 18, 2006, Endeavor entered into an Agreement by which it will acquire American Apparel. In exchange for all of the securities of the American Apparel companies outstanding immediately prior to the acquisition, Endeavor will issue 32,258,065 Transaction Shares, subject to downward adjustment based on American Apparel s net debt immediately prior to closing of the acquisition. 8,064,516 of the Transaction Shares will be placed into escrow to secure Endeavor s indemnity rights under the Agreement. The Agreement also provides for a $2,500,000 cash pool to be available for the granting of bonuses to management employees immediately following the closing of the acquisition. American Apparel also will be permitted to repay at the closing of the acquisition loans made to American Apparel by certain of its directors, officers and employees in an aggregate amount of approximately $5,000,000. Endeavor also will adopt a performance equity plan under which an aggregate of approximately 2,700,000 shares will be available for grant under options and restricted stock awards to employees.

In connection with Endeavor s initial public offering, it issued an option, for $100, to Ladenburg Thalmann to purchase 350,000 Units at an exercise price of $10.00 per Unit, with each Unit consisting of one share of common stock and one warrant. Endeavor accounted for the fair value of the option, inclusive of the receipt of the $100 cash payment, as an expense of the public offering resulting in a charge directly to stockholders equity. Endeavor estimated that the fair value of this option was approximately $703,500 ($2.01 per Unit) using a Black-Scholes option-pricing model. The fair value of the option granted to Ladenburg Thalmann was estimated as of the date of grant using the following assumptions: (1) expected volatility of 52.7%, (2) risk-free interest rate of 4.43%, (3) expected life of two years and 30 days and (4) dividend rate of zero. The option may be exercised for cash or on a cashless basis, at the holder s option, such that the holder may use the appreciated value of the option (the difference between the exercise prices of the option and the underlying warrants and the market price of the units and underlying securities) to exercise the option without the payment of any cash.

Table of Contents

BUSINESS OF AMERICAN APPAREL

Overview

American Apparel is a vertically-integrated manufacturer, distributor, and retailer of branded fashion basic apparel. As of September 30, 2007, American Apparel operated 165 retail stores in 13 countries, including the United States, Canada, Mexico, England, Germany, France, Italy, the Netherlands, Sweden, Switzerland, Israel, Japan and South Korea, either directly or through one or more subsidiaries. American Apparel also operates a leading wholesale business that supplies t-shirts and other casual wear to distributors and screen printers. In addition to its retail stores and wholesale operations, since 2004 American Apparel operates an online retail e-commerce website at *www.americanapparelstore.com*.

American Apparel currently has the following US-domiciled subsidiaries: American Apparel Retail, Inc., American Apparel Dyeing and Finishing, Inc., and KCL Knitting, LLC. Additionally, American Apparel operates its retail and wholesale business through the following direct and indirect foreign subsidiaries: American Apparel Canada Wholesale Inc., American Apparel Canada Retail Inc., American Apparel Deutschland GmbH, American Apparel Spain, S.L., American Apparel Italia GmbH, American Apparel (UK) Limited, American Apparel (Carnaby) Limited, American Apparel Mexico S DE RL DE CU, American Apparel Mexico Labor, LLC, American Apparel Japan Co., Ltd., American Apparel Korea Co., Ltd. and American Apparel Retail (Israel), Ltd.

American Apparel operates principally out of its 800,000 square foot facility in downtown Los Angeles, which houses its executive offices, as well as its cutting, sewing, and distribution operations. American Apparel operates a knitting facility in Los Angeles, as well as a dyeing and finishing facility in Hawthorne, California. The Company s domestic manufacturing operations allow American Apparel to quickly respond to customer demand and react faster to changing fashion trends. The Company s products are noted for their quality and fit, and the Company s edgy, distinctive branding has differentiated it in the marketplace. American Apparel® is a registered trademark of American Apparel, Inc.

American Apparel was founded in 1998 as a limited liability company in the state of California. In 2003, it was converted to a corporation. In 2004, it elected to be treated as a Subchapter S corporation. Since inception, American Apparel has operated its wholesale business. In October 2003, American Apparel opened its first retail store in Los Angeles. In 2004, American Apparel began its online retail operations, and opened its first stores in Canada and Europe. In 2005, it opened its first store in Asia.

Core Business Strengths

American Apparel has relied on a number of core business strengths that it believes have contributed to its past success and will contribute to its future growth:

Design Vision

American Apparel s design vision and aesthetic is intended to appeal to young, metropolitan adults by providing them with a core line of iconic, timeless styles offered year-round in a wide variety of colors at reasonable prices. Since its founding, American Apparel has operated with the belief that there is a large potential market among young adults for well-designed, high-quality, fashion essentials. Led by Mr. Charney, the Company s in-house creative team has carefully developed the Company s product line and brand image.

Advertising and Branding

American Apparel attracts customers through internally-developed, edgy, high-impact, visual advertising campaigns which use print, outdoor, in-store, and electronic communication vehicles. These advertising

campaigns communicate a distinct brand image that differentiates the Company from its competitors and seek to establish a connection with the company s customers. The company s retail stores are an important part of American Apparel s branding and convey a modern, internationalist lifestyle. At various times, the company has also drawn attention to the Made in USA nature of its products and the Sweatshop Free environment in which the company s garments are produced.

Speed to Market

The company s vertically integrated business model, where manufacturing and various other elements of the company s business processes are located in downtown Los Angeles, allows the company to play a role in originating and defining new and innovative trends in fashion, while enabling the company to quickly respond to market and customer demand for classic and new products. For the company s wholesale segment, being able to fulfill large orders with quick turn around allows American Apparel to win business that might otherwise go to competitors. The ability to respond to the market quickly means that the company s retail segment can deliver in-trend apparel in a timely manner, adhere to a policy of not discounting product at its retail stores and maximize sales on popular styles that may have otherwise sold out.

Quality

American Apparel prides itself on its use of quality fabrics. American Apparel has a stringent quality control department that oversees the production of its garments and, with the 2005 acquisition of its own dyeing operation, American Apparel has the ability to exercise greater control over the entire process of creating its expanding line of clothing and accessories.

Broad Appeal

While initially targeted towards young, metropolitan adults in North America, the clean, simple styles and quality of the company s garments have helped American Apparel appeal to various demographics across the world. The company believes that its appeal has been augmented by, and should continue to benefit from, the growing trend toward casual attire.

Growth Strategy

American Apparel has developed a growth strategy that is designed to capitalize on its strengths. The principal elements of this growth strategy are:

New Store Expansion

American Apparel is committed to expanding its presence in the North America while significantly increasing its store footprint in markets throughout Europe and Asia. American Apparel evaluates proposed sites based on traffic patterns, co-tenancies, average sales per square foot achieved by neighboring stores, lease economics, demographic characteristics and other factors considered important regarding the specific location. The company s experience in overseas markets to date suggests that American Apparel s brand concept is readily transferable.

New Merchandise Introduction

As American Apparel expands beyond its original product offering of t-shirts, the company is increasing the options available to its growing customer base. American Apparel has strategically expanded its product offerings and intends to continue to introduce new merchandise to complement its existing products and draw in new customers, including denim, sweaters, jackets, and other products.

Table of Contents

Continue In-Sourcing Manufacturing Processes

American Apparel has explored making strategic acquisitions to consolidate its manufacturing operations and continue to produce high quality products. In 2005, the company acquired a dyeing and finishing facility in Hawthorne, California. American Apparel believes that bringing certain elements of its production process in-house affords the company the opportunity to exert higher quality control while also lowering production costs. American Apparel intends to continue to pursue strategic opportunities to further consolidate its operations while maintaining its Made in USA status.

Improve Information Systems

American Apparel plans to implement an enterprise resources planning (ERP) system to replace, enhance and integrate many elements of its current information systems. The company currently operates a number of unrelated information technology systems which has resulted in operational inefficiencies and increased cost. It is anticipated that the implementation of this new system will be a multi-phased project, with the first phase covering manufacturing and production planning, and an estimated go-live date sometime in the first calendar quarter of 2008. Beyond the implementation of this ERP system, American Apparel believes that a continued focus on enhancing its information system will help optimize operations.

Manufacturing Operations

American Apparel conducts all of its manufacturing operations in the Los Angeles metropolitan area, and principally at its cutting and sewing facility in downtown Los Angeles.

American Apparel purchases yarn which is sent to knitters to be knit into greige fabric, which is fabric that is not dyed or otherwise processed. The company currently conducts knitting operations in-house at its knitting facility in Los Angeles. The company operates circular and flat knitting machines at this facility, producing jersey, piqué, fleece and ribbing using cotton and cotton/polyester yarns. The company also utilizes third-party commission knitters. The company s knitting facility knits approximately a third of the total fabric used in American Apparel s garments, and employs a staff of approximately 71 people, as of September 30, 2007.

Knitted greige fabric produced at the Los Angeles facility or other commission knitters is batched for bleaching and dyeing and is taken to the company s dyeing and finishing facility, or other local commission dyers. In some cases, dyed fabric is transferred to subcontractors for fabric laundering. The company s dyeing and finishing facility dyes approximately a third of the total fabric used in American Apparel s garments, and employs a staff of approximately 131 people, as of September 30, 2007.

All fabric is shipped to the company s primary manufacturing facility in downtown Los Angeles where it is inspected and eventually cut on manual and automated cutting tables, and subsequently sewn into finished garments. Some fabric is purchased directly from third parties, along with all trims. Garments are sewn by teams of sewing operators typically ranging from 5-15 operators, depending on the complexity of a particular garment. Each sewing operator performs a different sewing operation on a garment before passing it to the next operator. Sewing operators are compensated on a modified piece-rate basis. Quality control personnel inspect finished garments for defects and reject any defective merchandise. American Apparel also manufactures some hosiery in-house at this facility, where it does knitting, inspection, and packing, and uses off-site contractors for washing and boarding. Approximately 2,500 employees are directly involved in the cutting, sewing, and hosiery operations at the downtown Los Angeles facility, as of September 30, 2007.

American Apparel does not have any major suppliers for which it relies on the raw materials that it uses in its production process. Furthermore, the inputs that American Apparel purchases are produced competitively and are commodity in nature. American Apparel believes that it could easily source its inputs from other vendors if current suppliers were not able to meet its needs.

American Apparel maintains a warehouse and distribution center at its downtown Los Angeles facility where it stores fabric rolls, trims, and finished goods. The company also maintains warehouses in Montreal, Quebec, and Dusseldorf, Germany.

Retail

The retail segment consists of 165 retail stores in 13 countries, including the United States, Canada, Mexico, England, Germany, France, Italy, the Netherlands, Sweden, Switzerland, Israel, Japan and South Korea. American Apparel opened its first retail location in October 2003, in the Echo Park neighborhood of Los Angeles, California. American Apparel s retail segment principally targets young adults aged 21 to 32 through its unique assortment of fashionable clothing and accessories and its compelling in-store experience. American Apparel has established a reputation with its customers, who are culturally sophisticated, creative and independent-minded. The product offering includes women s and men s basic apparel and accessories, as well as new lines for children and pets. Stores average approximately 2,500-3,000 square feet of selling space. American Apparel s stores are located in large metropolitan areas, emerging neighborhoods, and select university communities.

American Apparel seeks to instill enthusiasm and dedication in store management personnel and sales associates through regular communication with the stores. Store personnel receive minimum hourly compensation and receive discretionary incentive compensation based on meeting sales and profitability benchmarks.

In September 2007, American Apparel began operations of a test retail concept named *California Vintage*, which sells fashionable vintage apparel not manufactured by American Apparel. Currently American Apparel operates one *California Vintage* location in Cologne, Germany. American Apparel has not yet determined its long-term plans for this concept.

Wholesale

The wholesale segment sells to over a dozen authorized distributors and 10,000 screen printers and advertising specialty companies. These screen printers and advertising specialty companies decorate our blank product with corporate logos, brands and other images. American Apparel s wholesale customers sell imprinted sportswear and accessories to a highly diversified range of end-consumers, including companies, sporting venues, concert promoters, athletic leagues, and educational institutions, among others. In order to better serve customers, American Apparel allows customers to order products by the piece, by the dozen, or in full case quantities. American Apparel also, to a lesser extent, fulfills custom and private-label orders. American Apparel does not have any major customers who account for ten percent or more of total consolidated or wholesale sales.

American Apparel operates a call center out of its Los Angeles headquarters. The call center is staffed with approximately 40 customer service representatives initiating sales calls, answering incoming phone calls, emails, and faxes assisting customers in placing orders, checking stock levels, looking for price quotes or requesting adjustments. On average, the call center receives 800 calls daily and operates from Monday to Friday, 7am to 6pm, PT.

While American Apparel operates primarily on a make-to-stock basis, manufacturing and maintaining a sufficient inventory of products to meet future demand, the company s in-house manufacturing capacity also allows American Apparel to fulfill large orders in a timely fashion. American Apparel levers its inventory position with a quick turn-around on customer orders. Credit approved orders to be shipped by ground service are generally shipped the same day when received before 4:30pm PT while those to be shipped by air are generally shipped the same day when received by 3:30pm PT. The majority of American Apparel s wholesale and internet consumer orders are processed within these parameters. For these reasons, American Apparel does not typically maintain a large backlog of orders.

Table of Contents

You can find more information about the financial results of each segment in American Apparel s consolidated financial statements included in this proxy statement.

Online Retail

Since 2004, American Apparel has operated an online retail e-commerce website at *www.americanapparelstore.com* which offers the company s products for purchase. This retail website has localized storefronts for many of the international markets in which American Apparel has a physical retail presence. In July 2007, American Apparel started operations of an online storefront for the Australian market.

Brand, Advertising, and Marketing

American Apparel s advertising and direct marketing initiatives have been developed to elevate brand awareness, increase customer acquisition and retention and support key growth strategies. American Apparel s in-house creative team works to create edgy, high-impact, provocative ads which are produced year-round and are featured in leading national and local lifestyle publications, on billboards, and on specialty online websites. American Apparel maintains a photo studio at its headquarters. Content for American Apparel s website and online store are also generated internally at American Apparel. While the primary intent of this advertising is to support American Apparel s retail and online retail segments, the wholesale segment also benefits from the greater overall brand awareness generated by this advertising.

For the wholesale segment, American Apparel takes advantage of industry trade shows as an opportunity to expand and enhance customer relationships, exhibit its product offerings and share new promotions with customers. American Apparel participates in approximately two dozen trade shows annually. American Apparel also produces an annual print catalog of its wholesale products, designed to be of the standard of high-end consumer retail catalogs with attractive models, appealing photographs and a clear display of products.

Product Development

American Apparel employs an in-house staff of designers and creative professionals whose mandate it is to develop compelling garments. Led by Mr. Charney, this team takes its inspiration from classic styles of the past, as well as the latest emerging trends in fashion seen on the streets of some of the most fashion-forward neighborhoods in the world. Even after a new style is launched, the American Apparel s design team will often continue to update or renew it.

Intellectual Property

American Apparel trademarks and service marks, and certain other trademarks, have been registered, or are the subject of pending trademark applications with the United States Patent and Trademark Office and with the registries of many foreign countries and/or are protected by common law. In the United States, American Apparel is the registered owner of the American Apparel, Classic Girl, Standard American, Classic Baby, and Sustainable Edition trademarks, among others.

Competition; Customers

The specialty retail, online retail and the wholesale apparel businesses are each highly competitive. The apparel industry is characterized by rapid shifts in fashion, consumer demand, and competitive pressures, resulting in both price and demand volatility. American Apparel believes that its emphasis on quality fashion essentials mitigates these factors.

American Apparel s retail segment competes on the basis of, among other things, the location of the stores, the breadth, quality, style, and availability of merchandise, the level of customer service offered and price. While American Apparel believes that the fit and quality of its garments, as well as the broad variety of colors and styles of casual fashion essentials that it offers, helps differentiate it, it competes against a wide variety of

Table of Contents

smaller, independent specialty stores, as well as department stores and national and international specialty chains. Companies that operate in this space include The Gap, Urban Outfitters, H&M, Uniqlo and Forever 21. Many of these companies have substantially greater name recognition as well as financial, marketing, and other resources.

The wholesale business competes with numerous wholesale companies based on the quality, fashion, availability, and price of our wholesale product offerings. These companies include Gildan Activewear, Hanes, Russell Athletic and Fruit of the Loom. Many of these companies have greater name recognition and financial and other resources.

Along with certain retail segment factors noted above, other key competitive factors for American Apparel s online retail operations include the success or effectiveness of customer mailing lists, response rates, merchandise delivery and web site design and availability. The online retail operations compete against numerous web sites, many of which may have a greater volume of web traffic, and greater financial, marketing and other resources**.**

Seasonality

American Apparel experiences seasonality in its operations. Historically, sales during the second and third fiscal quarters have generally been the highest, with sales during the first fiscal quarter the lowest. This reflects the combined impact of the seasonality of the wholesale and retail segments. Generally, American Apparel s retail segment has not experienced the same pronounced sales seasonality around the back-to-school and year-end holiday selling seasons as other retailers.

Employees

As of October 31, 2007, American Apparel employed a work force of over 6,100 employees worldwide. To ensure long-term success, American Apparel must attract, develop and retain skilled employees. This includes, but is not limited to manufacturing, retail, sales, creative, and executive employees. Competition for such employees can be intense. American Apparel s success is dependent to a significant degree on the continued contributions of key employees, including Mr. Charney.

American Apparel views its employees as long-term investments and adheres to a philosophy of providing employees with decent working conditions in a technology-driven environment which allows the company to attain improved efficiency, while inspiring employee loyalty. American Apparel has emphasized its compensation structure and benefits package for manufacturing employees, which includes above-market wages, company-subsidized health insurance, free English language classes, free massage, free parking, as well as other benefits. American Apparel also provides for a well-lit working environment that is properly ventilated and heated or cooled in its manufacturing facilities. These working conditions, as well as compensation and benefits packages, are key elements in achieving American Apparel s desire to be an employer of choice in the Los Angeles area. American Apparel tries to provide for year-round employment, in contrast to the seasonality in production volumes experienced by other apparel companies which often result in seasonal layoffs. None of the employees are covered by a collective bargaining agreement. American Apparel has never had a strike and believes that its relations with its employees are excellent.

Information Technology

American Apparel is committed to utilizing technology to enhance its competitive position. American Apparel s information systems provide data for production, merchandising, distribution, retail stores and financial systems. The core business systems, which consist of both purchased and internally developed software, are accessed over a company-wide network providing corporate employees with access to key business applications.

To support continued growth, American Apparel has initiated a strategic review of its information systems. American Apparel plans to implement the ERP system to replace, enhance and integrate many elements of its

Table of Contents

current information systems. American Apparel currently operates a number of unrelated information technology systems that have resulted in operational inefficiencies and in some cases have increased costs. It is anticipated that the implementation of this new system will be a multi-phased project, with the first phase covering manufacturing and production planning, with an estimated go-live date sometime in the first quarter of calendar 2008. If American Apparel fails to properly execute or misses critical deadlines in the implementation of this new system, it could experience serious disruption and harm to its business.

American Apparel dedicates a significant portion of its information technology resources to web services, which includes the operation of the corporate website at *www.americanapparel.net* and the online retail site at *www.americanapparelstore.com*.

Properties

The following table sets forth the location and use of each of American Apparel s principal non-retail properties, which are all leased:

Location	Use
Los Angeles, California	Executive offices, sewing, cutting, and distribution
Los Angeles, California	Knitting facility
Hawthorne, California	Dyeing and finishing facilities
Montreal, Quebec	Executive offices, distribution
Dusseldorf, Germany	Offices, distribution
London, England	Offices
Tokyo, Japan	Offices
Seoul, South Korea	Offices

144

Table of Contents

All of American Apparel s retail stores are well maintained and in good operating condition. American Apparel s retail stores are typically leased for a term of five to ten years with renewal options for an additional five to ten years. Most of these leases provide for base rent, as well as maintenance and common area charges, real estate taxes and certain other expenses. Selling space of opened stores will sometimes change due to store renovations that modify space utilization, use of staircases, cash registers configuration, and other factors. As well, a number of American Apparel store locations have undergone expansions in the past several years. The following table shows the location of each of American Apparel s existing retail stores, as of September 30, 2007:

Domestic Locations (96)

Arizona (2)

Tempe

Tuscon

California (24)

Berkeley

Camarillo

Claremont

Los Angeles

- Cherokee
- Factory Store
- Echo Park
- Hollywood
- Little Tokyo
- Los Feliz
- Melrose
- Robertson
- Westwood Village
- West Hollywood

Huntington Beach

La Jolla

Colorado (2)

Boulder

Denver

Connecticut (1)

South Norwalk

District of Columbia (1)

Lincoln Square

Florida (7)

Coconut Grove

Coral Gables

Gainesville

Key West

Miami

- Lincoln Road
- Ocean Drive
- Sunset Drive

Georgia (4)

Louisiana (1)

New Orleans

Maryland (2)

Baltimore

Silver Spring

Massachusetts (2)

Boston

Cambridge

Michigan (3)

Ann Arbor

East Lansing

Royal Oak

Minnesota (1)

Minneapolis

Nevada (1)

Las Vegas

New York (cont d.)

- Columbus Circle
- Flatiron
- Gramercy Park
- Lower East Side
- Soho
- Tribeca
- Upper East Side
- West Village

Woodbury Common

North Carolina (1)

Charlotte

Ohio (3)

Cincinnati

Cleveland

Columbus

Oregon (3)

Eugene

Rhode Island (1)

Providence

South Carolina (2)

Charleston

Columbia

Tennessee (2)

Memphis

Nashville

Texas (2)

Dallas

Houston

Vermont (1)

Burlington

Virginia (1)

Richmond

Palo Alto	Atlanta		Portland	*Washington (3)*
San Diego	Buckhead	*New Jersey (1)*	Hawthorne Blvd.	Seattle
Hillcrest	Georgia Tech	Hoboken	Stark Street	Capitol Hill
Pacific Beach	Little Five Points			Downtown Seattle
San Francisco	Savannah	*New York (16)*	*Pennsylvania (4)*	University Way
Haight Ashbury		Brooklyn	Philadelphia	
Union Street	Illinois (5)	Carroll Gardens	Sansom Commons	
Santa Ana	Chicago	Court Street	Walnut Street	
Santa Barbara	Gold Coast	Park Slope	Pittsburgh	
Santa Cruz	Lakeview	Williamsburg	Shadyside	
Santa Monica	Lincoln Park	Manhattan	Univ. of Pittsburgh	
	Wicker Park	Broadway		
	Evanston	Chelsea		
		Columbia University		

Table of Contents

International Locations (69)

Canada (25)

Alberta (2)

Calgary

Edmonton

British Columbia (4)

Burnaby

Vancouver

Granville

South Granville

West 4th Street

Nova Scotia (1)

Halifax

Ontario (8)

Kingston

Ottawa

Toronto

Bloor Street

Church Street

College Street

Queen Street

Quebec (10)

Montreal

Cote-des-Neiges

Cours Mont-Royal

Mont-Royal Est

St-Denis

St-Laurent

Ste-Catherine

Ste-Catherine Est

Pointe-Claire

Sainte-Foy

Westmount

Mexico (2)

Mexico City

Playa del Carmen

Europe (30)

France (6)

Paris

Be aurepaire

Marais Men s

Marais Women s

Marche St-Honore

Saint-Germain

Vielle du Temple

Germany (14)

Berlin 1

Berlin 2

Berlin 3

Cologne 1

Cologne 2

(California Vintage)

Dusseldorf

Frankfurt

Hamburg

Hamburg 2

Heidelberg

Munich 1&2

Italy (1)

Milan

Netherlands (2)

Amsterdam

Rotterdam

Sweden (1)

Stockholm

Switzerland (1)

Zurich

United Kingdom (5)

Brighton

London

Carnaby Street

Kensington

High St.

Portobello Road

Shoreditch

Israel (1)

Tel Aviv

Asia (11)

Japan (5)

Fukuoka

Osaka

Tokyo

Azabu

Daikanyama

Shibuya

South Korea (6)

Bundang

Busan

Cheong-Ju

Seoul

Hong-Dae

Kangnam

Myung-Dong

Yonge & Dundas	Munich 3
Yonge & Eglington	Stuttgart

Stores Opened by Year

	United States	Canada	International	Total
2003				
Opened	3	1	0	4
Total at Year End	3	1	0	4
2004				
Opened	22	8	3	33
Total at Year End	25	9	3	37
2005				
Opened	41	11	15	67
Total at Year End	66	20	18	104
2006				
Opened	29	6	12	47
Closed	(2)	0	0	(2)
Total at Year End	93	26	30	149
2007				
Opened	4	0	14	18
Closed	(1)	(1)	0	(2)
Total as of September 30, 2007	96	25	44	165

Table of Contents

Store Pipeline

As part of American Apparel s new store expansion, at any one time American Apparel may have store locations under signed leases which are in the process of being opened. This store pipeline as of September 30, 2007 is as follows:

Austin, TX	Las Vegas, NV	Scottsdale, AZ	Barcelona, Spain	London, England
Honolulu, HI	Pasadena, CA	Vancouver, BC	Florence, Italy	Covent Garden
Kansas City, MO	Salt Lake City, UT	Winnipeg, MB	Glasgow, Scotland	Oxford Street
King of Prussia, PA	San Francisco, CA	Antwerp, Belgium	Jerusalem, Israel	Madrid, Spain
				Turin, Italy

Comparable Same Store Sales

Comparable same store sales are defined as the change in sales for stores that have been open for more than one year over the comparable period of the previous year. The table below shows the comparable same store sales of American Apparel, including the number of stores included in the comparison at the end of each period and the increase from the prior comparable period.

	For the Quarter Ended				
	March 31	**June 30**	**September 30**	**December 31**	**Year to date**
2005	64%	56%	41%	41%	45%
Stores	6	10	18	31	
2006	16%	0%	3%	5%	5%
Stores	43	50	64	83	
2007	17%	24%	27%		
Stores	104	119	131		

Environmental Regulation

American Apparel s operations are subject to various environmental and occupational health and safety laws and regulations. Because the company monitors, controls and manages environmental issues, American Apparel believes it is in compliance in all material respects with the regulatory requirements of those jurisdictions in which its facilities are located as it does receive compliance confirmations from those jurisdictions on a regular basis. In line with its commitment to the environment as well as to the health and safety of its employees, American Apparel will continue to make expenditures to comply with these requirements, and does not believe that compliance will have a material adverse effect on its business. As is the case with manufacturers in general, if a release of hazardous substances occurs on or from its properties or any associated offsite disposal locations, or if contamination from prior activities is discovered at any of its properties, American Apparel may be held liable. While the amount of such liability could be material, American Apparel seeks to conduct its operations in a manner that reduces such risks.

Legal Proceedings

American Apparel is subject to regulatory inquiries, claims and suits that arise in the ordinary course of business and is, from time to time, involved in litigation incidental to the conduct of its business. Additionally, from time to time, American Apparel is the subject of labor related claims filed by current and former employees with the courts and regulatory agencies. The company conducts extensive internal investigations of all allegations brought against it and cooperates with external regulatory investigations.

During the latter half of 2006, American Apparel initiated company-wide layoffs in response to its then-current financial condition. One of the employees affected by these layoffs was Mr. Lewis Copsidas, an accounts receivable manager for American Apparel. During the first quarter of 2007, American Apparel was contacted in

147

writing by Mr. Copsidas, who alleged that his termination was due to his age. American Apparel promptly conducted an internal investigation of the allegation and found no evidence to support any such claim. In June 2007, Mr. Copsidas filed a claim with the Equal Employment Opportunity Commission (EEOC), which is currently investigating the claim. Upon request, American Apparel submitted a written statement to the EEOC in support of its position with respect to Mr. Copsidas termination in July 2007. No further action has been taken by the EEOC or Mr. Copsidas. To the best of American Apparel s knowledge, Mr. Copsidas has not specified any damages nor sought any specific relief in his pending EEOC claim.

Additionally, on or about September 19, 2005, Ms. Mary Nelson, an independent contractor in the sales department at American Apparel commenced a suit in a case captioned as *Mary Nelson v. American Apparel, Inc., et al*., Case Number BC333028, filed in Superior Court of the State of California for the County of Los Angeles, Central District, wherein she alleges she was wrongfully terminated, was subjected to harassment and discrimination based upon her gender and other claims related to her tenure at American Apparel. The company denies all of Ms. Nelson s allegations of wrongdoing. Ms. Nelson is seeking unspecified monetary damages and costs. This case is currently in pre-trial mediation. American Apparel intends to aggressively defend this matter.

On or about September 4, 2007, Hanesbrands, Inc. and related entities (collectively, Hanes) filed a lawsuit in the United States District Court for the Middle District of North Carolina captioned *Hanesbrands, Inc. et al. v. American Apparel, Inc. and American Apparel Retail, Inc.,* Case No. 1:07-cv-00662. In that lawsuit, Hanes contends that American Apparel used Hanes trademarks BARELY THERE and/or BARELYTHERE without Hanes authorization or approval and, by so doing, falsely represented the source, affiliation or sponsorship of American Apparel products. American Apparel is in the process of settling this matter with Hanes and does not expect the settlement to be material, however, no determination can be made at this time as to the final outcome of the settlement.

On or about October 3, 2007, Ms. Sonja Klimp filed a lawsuit in the United States District Court for the Central District of California captioned as *Sonja Klimp v. American Apparel, Inc. and American Apparel Retail, Inc.*, Case No. CV07-06448. Ms. Klimp is claiming that American Apparel, Inc. and American Apparel, Retail, Inc., knowingly and willfully violated the Fair Credit Reporting Act (15 U.S.C. §1681 et seq.) by printing more than the last five digits of a person s credit card or debit card numbers and/or printing the expiration date of the person s credit card on receipts provided to customers. The lawsuit is seeking an order certifying this case as a class action, as well as injunctive relief and unquantified statutory and monetary damages. American Apparel denies the allegations and intends to aggressively defend this matter.

American Apparel s management intends to investigate all of the aforesaid matters and, as appropriate, engage in a vigorous defense. Although the outcome of these claims cannot be determined with certainty, American Apparel is of the opinion that these claims will not have a material adverse impact on American Apparel s financial position, results of operations or liquidity. However, management s assessment of American Apparel s exposure could change as the claims proceed or if additional facts become known in the future.

Compensation Discussion and Analysis

Discussion and Analysis of Current Compensation Scheme

Since its formation, American Apparel has been a closely held company, operating under the direction of its Chief Executive Officer and its board of directors (which consists of the Chief Executive Officer and Mr. Lim, the company s Secretary). As a result, American Apparel s executive compensation practices have been relatively informal. To date, American Apparel has not used, and has not had the need to use, the more formal compensation practices and policies employed by publicly traded companies subject to the executive compensation disclosure rules of the Securities and Exchange Commission. Historically, all compensation decisions have been made by American Apparel s Chief Executive Officer, with the approval and consent of the board of directors when deemed necessary or appropriate.

Table of Contents

American Apparel s Chief Executive Officer and Secretary are the sole shareholders of American Apparel, a subchapter S corporation, and, in lieu of salary or other compensation, have elected to take periodic cash distributions of the net income of the company allocated to them as shareholders of a subchapter S corporation.

The primary goals of American Apparel s executive compensation program for other executives are to attract and retain the most talented and dedicated executives possible through the use of a cash incentives designed to reward the achievement of corporate and individual objectives that promote the growth of American Apparel s business. American Apparel s compensation packages for the executives other than Mr. Charney and Mr. Lim have generally been a mix of salary and cash incentive payments. American Apparel has not employed equity based compensation for such other executives because of its belief that, due to the illiquid nature of an investment in its shares, equity based compensation would not provide the same incentive as a cash-based program.

American Apparel believes that its performance-based compensation is an important component of the total executive compensation package for attracting, motivating and retaining high-quality executives.

American Apparel s compensation philosophy is designed to help the company attract talented individuals to manage and operate all aspects of its business, to reward these individuals fairly, and to retain those individuals who continue to meet American Apparel s high expectations and support the achievement of its business objectives. In this regard, during 2006, American Apparel s compensation program was designed to:

- reward employees and executives for the company s overall performance; and

- attract and retain talented individuals who are capable of leading American Apparel as it continues to develop into a preeminent clothing manufacturer and retail enterprise.

Elements of Compensation

The compensation received by American Apparel s executive officers consists of the following elements:

Compensation of Messrs. Charney and Lim. In lieu of salary and other compensation, during 2006 Messrs. Charney and Lim, received periodic cash distributions of the net income of the company allocated to them under the subchapter S corporation rules. During 2006, Mr. Charney received distributions in the amount of $348,000 and Mr. Lim received distributions in the amount of $348,000. During 2006, Mr. Charney also borrowed $69,468 and Mr. Lim borrowed $148,580 from the company. Mr. Charney also received a management fee from the CI companies in the amount of USD$2,045,000. To date, during 2007, Messrs. Charney and Lim have each received distributions in the amount of $2,260,920 from the company. Additionally, during 2007 Mr. Charney has borrowed $439,947 and Mr. Lim has borrowed $238,098 from the company. Mr. Charney has also had approximately USD$2.7 million in management fees allocated to him from the CI companies. These management fees are subject to adjustment based upon the full year performance of the CI companies.

Compensation of other Executive Officers.

Base Salary. Base salaries for American Apparel s other executive officers are established based on the scope of their responsibilities, historical performance and individual experience. Base salaries are reviewed annually, and adjusted from time to time. During 2006:

- Ken Cieply, American Apparel s Chief Financial Officer commencing June 12, 2006, received a salary of $103,846; and

- Martin Bailey, American Apparel s President of Manufacturing, received a salary of $200,000 and a bonus of $15,000 for a total of $215,000.

The base salaries for Messrs. Cieply and Bailey have increased during 2007. Mr. Cieply s current annual salary is $240,000 (a 20% increase) and Mr. Bailey s current salary is $245,000 (a 22.5% increase).

149

Table of Contents

Benefits. AAI also offers the following benefits to its named executive officers, generally on the same basis provided to all of its employees:

- health, dental insurance and vision;
- life insurance; and
- short-term disability.

Discussion and Analysis of Future Compensation Scheme

Overall

Following completion of the transactions contemplated by the Acquisition Agreement, American Apparel intends to develop executive compensation packages that are competitive in terms of potential value to its executives, and which are tailored to the unique characteristics and needs of American Apparel within its industry to reward its executives for their roles in creating value for shareholders. American Apparel intends to be competitive with other similarly situated companies in its industry following completion of the acquisition.

It is anticipated that decisions on executive compensation policies and programs following the completion of the acquisition will be made by a compensation committee of the company s Board of Directors Since that compensation committee will not be established until consummation of the acquisition, no formal or informal policies or guidelines now exist for allocating compensation between long-term and currently paid out compensation, between cash and non-cash compensation, or among different forms of compensation have been adopted as of the date hereof. The following discussion is based on the company s present expectations as to the policies and programs to be adopted by the compensation committee. The actual policies and programs actually adopted will depend on the application of the judgment of the members of the compensation committee and may differ from those reflected in the following discussion.

Of necessity, the compensation decisions regarding executives will be based on the need to retain and attract individuals with the skills necessary for the company to achieve its business objectives, to reward those individuals fairly, and to retain those individuals who continue to perform at or above expectations.

It is anticipated that compensation for executives will have three primary components salary, cash incentive bonus and stock-based awards. These components of executive compensation would be related but distinct. Although it is anticipated that the compensation committee would review total compensation, the company does not believe that significant compensation derived from one component of compensation should negate or reduce compensation from other components. The company anticipates determining the appropriate level for each compensation component based in part, but not exclusively, on its view of internal equity and consistency, individual performance and other information deemed relevant and timely.

In addition to the guidance provided by its compensation committee, the company may utilize the services of third parties from time to time in connection with the hiring and compensation awarded to executive employees. This could include subscriptions to executive compensation surveys and other databases.

It is expected that the compensation committee will be charged with performing an annual review of executive officers cash compensation and equity holdings to determine whether they provide adequate incentives and motivation to executive officers and whether they adequately compensate the executive officers relative to comparable officers in other companies.

Benchmarking of Cash and Equity Compensation

The company expects that the compensation committee will stay apprised of the cash and equity compensation practices of publicly held companies in the apparel and related industries through data obtained from such companies public reports and from other resources. It is expected that any companies chosen for

150

Table of Contents

inclusion in any benchmarking group would have business characteristics comparable to the company, including revenues, financial growth metrics, stage of development, employee headcount and market capitalization. While benchmarking may not always be appropriate as a stand-alone tool for setting compensation due to the aspects of the post-acquisition business and objectives that may be unique to the company, The company expects gathering this information will be an important part of its compensation-related decision-making process.

Compensation Components

Base Salary. The company expects to work with the compensation committee to set executive base salaries at levels comparable with those of executives in similar positions and with similar responsibilities at comparable companies. The company expects to maintain base salary amounts at or near the industry norms while avoiding paying amounts in excess of what it believes is necessary to motivate executives to meet corporate goals. It is anticipated that base salaries will generally be reviewed annually, subject to terms of employment agreements, and that the compensation committee and board will seek to adjust base salary amounts to realign such salaries with industry norms after taking into account individual responsibilities, performance and experience.

Annual Bonuses. The company intends to utilize cash incentive bonuses for executives to focus them on achieving key operational and financial objectives within a yearly time horizon. It expects that, near the beginning of each year, the board, upon the recommendation of the compensation committee and subject to any applicable employment agreements, will determine performance parameters for appropriate executives. It also expects that, at the end of each year, the board and compensation committee will determine the level of achievement for each corporate goal.

It is anticipated that the performance parameters for eligibility to receive cash bonuses under the terms of the employment agreements to be executed in connection with the consummation of the acquisition will be set by the compensation committee each year, within 45 days of approval of such year s annual budget.

The company intends to establish cash incentive bonus compensation that it is taxable to its employees at the time it becomes available to them. At this time, it is anticipated that one or more executive officer s annual cash compensation may exceed $1 million, and Endeavor may make plans to qualify for any compensation deductions under Section 162(m) of the Internal Revenue Code (the Code).

Equity Awards. The company also intends to use stock options and other stock-based awards to reward long-term performance. The company believes that providing a meaningful portion of an executive s total compensation package in stock options and other stock-based awards will align the incentives of its executives with the interests of shareholders and with the company s long-term success. The company expects the compensation committee and board to develop their equity award determinations based on their judgments as to whether the complete compensation packages provided to executives, including prior equity awards, are sufficient to retain, motivate and adequately award the executives.

Equity awards will be granted through the 2007 Performance Equity Plan, which was adopted by Endeavor board and is being submitted to the stockholders of Endeavor for their consideration at the special meeting. All employees, directors, officers and consultants will be eligible to participate in the 2007 Performance Equity Plan. The material terms of the 2007 Performance Equity Plan are further described in the section of this proxy statement entitled 2007 Performance Equity Plan Proposal. No awards have been made under the plan as of the date of this proxy statement. It is anticipated that all options granted under the plan in the future will have an exercise price at least equal to the fair market of Endeavor s common stock on the date of grant.

Any equity compensation expense will be accounted for under the rules of Statement of Financial Accounting Standard (SFAS) No. 123R, which requires a company to estimate and record an expense for each award of equity compensation over the service period of the award. Accounting rules also will require the company to record cash compensation as an expense at the time the obligation is accrued. Until the company achieves sustained profitability, the availability to it of a tax deduction for compensation expense is not material to its financial position.

Table of Contents

Severance Benefits. The company may consider the adoption of a severance plan for executive officers and other employees in the future. Employment agreements that may be entered into by the persons who will initially serve as executive officers following consummation of the acquisition will likely provide for certain rights and obligations in the event of the termination of employment as more fully described in the section of this proxy statement entitled Employment Agreements.

Other Compensation. It is currently anticipated that the company will establish and maintain various employee benefit plans, including medical, dental, life insurance and 401(k) plans. These plans will be available to all salaried employees and will not discriminate in favor of executive officers. The company may extend other perquisites to its executives that are not available to its employees generally.

For additional information regarding the compensation philosophy and objectives, elements of compensation, and material factors used by the compensation committee with respect to ongoing compensation of executive officers following the consummation of the acquisition, see the section entitled *Directors and Executive Officers of Endeavor Following the Acquisition Executive Compensation.*

Summary Compensation

The following table shows for 2006, compensation awarded or paid to, or earned by, American Apparel s principal executive officer, its principal financial officer and its next three most highly compensated executive officers in 2006 who received at least $100,000 of total compensation. We refer to such persons elsewhere in this document as American Apparel s named executive officers.

Summary Compensation Table

Name and Principal Position	Year	Owner Distributions	Salary ($)	Bonus ($) (1)	All Other Compensation	Total
Dov Charney *President and Chief Executive Officer*	2006	$ 348,000(2)	$ 2,045,000(3)	$	$ 33,726(4)	$ 2,426,726
Ken Cieply(5) *Chief Financial Officer*	2006		$ 103,846	$ 10,000	$ 22,572(6)	$ 136,418
Sam Lim *Secretary*	2006	$ 348,000(2)	$ 0	$	$ 40,754(7)	$ 388,754
Martin Bailey *President of Manufacturing*	2006		$ 200,000	$ 15,000	$ 55,322(8)	$ 270,322

(1) Includes bonuses earned in 2006, regardless of when paid.

(2) Messrs. Charney and Lim did not receive any salary or bonus from American Apparel in connection with their service as executive officers of the Company. As shareholders of AAI, and as a result of the S corporation status of the company, each of Messrs. Charney and Lim are allocated income based on the net profits of the company and , from time to time, received a distribution of the profits attributed to each of them. During 2006, Mr. Charney received distributions on his allocable income in the amount of $348,000 and Mr. Lim received on his allocable income in the amount of $348,000.

(3) Under the terms of an arrangement among the CI companies and Mr. Charney, Mr. Charney received a management fee of (USD$) $2,045,000.

(4) Personal benefits include payment of the executive officer s share of the Company s health insurance premium. The total also includes $31,608 in life insurance premiums paid on behalf of life insurance policies held by Mr. Charney. American Apparel is also the beneficiary of one or more key-man insurance policies issued for Mr. Charney. The face value of these policies is $50 million.

(5) Mr. Cieply joined AAI on June 12, 2006. His annualized salary for 2006 was $200,000.

152

Table of Contents

(6) Personal benefits include commuting reimbursement expenses related to Mr. Cieply s commute between Montreal, Canada and Los Angeles, California.

(7) Personal benefits include payment of the executive officer s share of the Company s health insurance premium and a vehicle reimbursement expense of $14,631. The total also includes $15,000 in life insurance premiums paid on behalf of a life insurance policy held by Mr. Lim.

(8) Personal benefits include payment of the executive officer s share of the Company s health insurance premium and a vehicle allowance. The total also includes $24,000 in life insurance premiums paid on behalf of life insurance policies held by Mr. Bailey.

Pension Benefits

American Apparel s named executive officers did not participate in, or otherwise receive any benefits under, any pension or retirement plan sponsored by the company during 2006.

Nonqualified Deferred Compensation

American Apparel s named executive officers did not earn any nonqualified compensation benefits from the company during 2006.

Employment Agreements

American Apparel has not entered into any employment agreements or other written employment arrangements with any of its named executive officers. However, in contemplation of the transactions contemplated by the Acquisition Agreement, Endeavor has entered into an agreement with Mr. Charney. For a further discussion of this agreement, see the section entitled *Directors and Executive Officers of Endeavor Following the Acquisition Executive Compensation Employment Agreement and Non-Competition Covenants.*

Severance Arrangements

American Apparel has not entered into any change in control agreements or other severance arrangements with any of its named executive officers.

Director Compensation

Currently, Messrs. Charney and Lim are the sole members of the American Apparel board of directors. Neither Mr. Charney nor Mr. Lim receive any cash or non-cash compensation for their services as members of the board. Further, neither Mr. Charney nor Mr. Lim is reimbursed for any expenses incurred in connection with their attendance at board of directors meetings. For information regarding director compensation following the consummation of the acquisition, see the section entitled *Directors and Executive Officers of Endeavor Following the Acquisition Compensation of Directors.*

Table of Contents

AMERICAN APPAREL S MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The information contained in this section has been derived from consolidated financial statements of AAI, the combined financial statements of CI companies. Information contained herein should be read together with AAI s, and the CI companies financial statements and related notes included elsewhere in this proxy statement.

The following discussion is intended to assist in the assessment of significant changes and trends related to the results of operations and financial condition of American Apparel. This discussion and analysis should be read in conjunction with AAI s consolidated financial statements and notes thereto included, as well as in conjunction with the CI companies combined financial statements and notes thereto included.

American Apparel s business has grown organically in all of its markets. AAI designs, manufactures and distributes apparel for women, men, children and pets in retail stores and through wholesale business operations, which includes its web-based operations, throughout the United States and internationally, except for Canada where the CI companies sell AAI s products through their retail stores and distribute goods to third party wholesale companies.

American Apparel s revenue is driven by its ability to design and market desirable products, identify business opportunities and secure new as well as renew existing distribution channels. American Apparel s income from operations is derived from its ability to generate revenue and collect cash in excess of labor, material and other inventory manufacturing costs as well as selling, general and administrative costs.

US and Canadian dollar amounts set forth in American Apparel s Management s Discussion and Analysis of Financial Conditions and Results of Operations are in thousands (000s) unless otherwise indicated.

Nature of Operations

AAI is a designer, manufacturer and distributor of blank t-shirts and other comfort apparel for men, women, children and pets. AAI operates its business through three distinct business segments: US Wholesale, which includes a consumer e-commerce web site; US Retail, which consists of 96 retail stores located in the United States; and International (International represents the All other category which is comprised of international retail, international wholesale and international online operations) consisting of 44 retail stores in 12 countries, several international e-commerce websites and some wholesale activity . AAI maintains corporate offices, primary manufacturing and distribution facilities, as well as a knitting and dye house in Los Angeles, California. AAI also maintains a portion of its yarn at outside knitting facilities and a portion of its greige goods at outside dye houses. AAI operates through numerous subsidiaries. AAI s net sales from US Wholesale, US-Retail, and International, as a percentage of consolidated net sales, were approximately 45.4%, 31.5% and 23.1%, for the nine months ended September 30, 2007 53.5%, 29.5% and 17.0% for the nine months ended September 30, 2006, and 52.2%, 30.3% and 17.5% for the twelve months ended December 31, 2006. The CI companies sell American Apparel products through 25 Canadian retail outlets, as well as a Canadian wholesale distribution center.

During the period from January 1, 2004 through September 30, 2007, American Apparel increased its US-based retail stores from three to 96, while establishing an additional 69 retail outlets in 13 countries. The following tables detail the growth in retail store activity during the nine months ended September 30, 2007 and twelve months ended December 31, 2006, 2005 and 2004.

Retail Stores US	9 Months September 30, 2007	9 Months September 30, 2006	12 Months December 31, 2006	12 Months December 31, 2005	12 Months December 31, 2004
Open at beginning of the period	93	66	66	26	3
Opened during the period	4	24	29	40	23
Closed during the period	(1)	0	(2)	0	0
Open at end of the period	96	90	93	66	26

Retail Stores - International	9 Months September 30, 2007	9 Months September 30, 2006	12 Months December 31, 2006	12 Months December 31, 2005	12 Months December 31, 2004
Open at beginning of the period	30	18	18	3	0
Opened during the period	14	10	12	15	3
Closed during the period	0	0	0	0	0
Open at end of the period	44	28	30	18	3

Retail Stores - Canadian	9 Months September 30, 2007	9 Months September 30, 2006	12 Months December 31, 2006	12 Months December 31, 2005	12 Months December 31, 2004
Open at beginning of the period	26	20	20	9	1
Opened during the period	0	4	6	11	8
Closed during the period	(1)	0	0	0	0
Open at end of the period	25	24	26	20	9

Overview

For the nine months ended September 30, 2007 AAI reported net sales of $255 million, an increase of $58 million over the comparable 2006 period. Further, the CI companies posted net sales of CDN$33 million for the nine months ended September 30, 2007, up from CDN$26 million for the corresponding 2006 period. The increase in net sales was generally the result of expansion in the company s US Retail, International and Canadian retail distribution channels, as the company added new store locations and expanded its product offerings in existing stores. American Apparel selects new store locations based upon consideration of a number of factors, including projected sales potential, financial conditions of the prospective lease agreement, co-tenancy, as well as ancillary benefits such as increase in brand recognition. At times, consideration is also given to locations where American Apparel has no retail store presence but on-line sales history demonstrates a strong demand for the products. During the period, American Apparel expanded its fabric offerings which facilitated introduction of new styles across the wholesale and retail distribution channels. As many as thirty new styles were added to the retail distribution channel of which the most notable was the addition of denim products. As a result, AAI and the CI companies both saw comparable store sales increase by 24% as compared to the prior like nine month period.

Gross profits for AAI and the CI companies increased by 7.2 percentage points and 1 percentage point, respectively, in the nine-month period ended September 30, 2007 as compared to the first nine months of 2006. These increases are primarily attributed to the higher mix of retail sales to wholesale sales which generate higher gross profits. A higher percentage of sales were from retail sales with a lower cost of sales percentage due to higher sales price at retail compared to wholesale. AAI s net income for the 2007 period increased to $11.6 million compared to a loss of $0.2 million in the 2006 period, while the CI companies reported net income of CDN$1 million for the nine months ended September 30, 2007 as compared to CDN$0.1 million in the corresponding 2006 period.

Management of American Apparel believes that this growth has been enhanced by the addition of new stores, an increased focus on building brand awareness and product diversity, designed to keep existing retail customers and attract new ones. To build on this trend, American Apparel is looking to grow its US Retail, International and Canadian Retail segments. 13 additional stores are expected to open before the end of 2007 domestically and internationally. Additionally, AAI and the CI companies are currently selecting, negotiating and reviewing new store leases slated for openings in 2008.

As American Apparel s business grows, management is examining its existing systems to make each segment work as efficiently as possible. To that end, the first phase of the company s ERP system to manage the production requirements is expected to go operational in the first quarter of 2008. The new ERP system will

Table of Contents

enable AAI to handle higher production volume through more efficient supply chain management. AAI, while currently able to meet its production requirements using both internal and third party resources, is developing strategies to increase its internal production capacity to meet future needs. The business combination with Endeavor will provide additional working capital that is needed for the company to achieve its current expansion goals. However, in the event that the Endeavor shareholders fail to approve the contemplated transactions, American Apparel would likely be required to scale back its expansion plans.

Critical Accounting Estimates and Policies

Complete descriptions of American Apparel s significant accounting policies are outlined in Note 2 of the *Notes to Consolidated Financial Statements* included in this proxy statement.

The preparation of financial statements in conformity with GAAP in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. American Apparel s critical accounting estimates and policies include:

- sales returns and allowances;
- allowance for doubtful accounts; inventory valuation and obsolescence;
- valuation and recoverability of long-lived and indefinite-lived intangible assets including the values assigned to acquired intangible assets, goodwill, and property, plant and equipment;
- income taxes;
- foreign currency; and
- accruals for the outcome of current litigation.

In general, estimates are based on historical experience, on information from third party professionals and on various other sources and assumptions that are believed to be reasonable under the facts and circumstances at the time such estimates are made. On a continual basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews, and if deemed appropriate, those estimates are adjusted accordingly. Actual results may vary from these estimates and assumptions under different and/or future circumstances. American Apparel s management considers an accounting estimate to be critical if:

- it requires assumptions to be made that were uncertain at the time the estimate was made; and
- changes in the estimate, or the use of different estimating methods that could have been selected, could have a material impact on American Apparel s consolidated results of operations or financial condition.

Revenue Recognition

American Apparel recognizes product sales revenue when title and risk of loss have transferred to the customer, there is persuasive evidence of an arrangement, shipment and passage of title has occurred, the sales price is fixed or determinable and collectibility is reasonably assured. Revenue from wholesale sales, are recorded at the time the product is shipped to the customer. Revenue from online sales are recorded at the time the products are delivered to the customers. With respect to its own retail store operations American Apparel recognizes revenue upon the sale of its products to retail customers. American Apparel s net sales represent gross sales invoiced to customers, less certain related charges for discounts, returns, and other promotional allowances. Allowances provided for these items are presented in the consolidated financial statements primarily as

156

reductions to sales and cost of sales (see Sales Returns and Other Allowances discussed below for further information). American Apparel recognizes the sales from gift cards, gift certificates and store credits as they are redeemed for merchandise.

Allowance for Sales Returns

American Apparel analyzes sales returns in accordance with SFAS No. 48 Revenue Recognition When Right of Return Exists (SFAS 48). American Apparel is able to make reasonable and reliable estimates of product returns for both its wholesale and retail segments based upon historical experience. American Apparel also monitors the buying patterns of the end-users of its products based on sales data received by its retail outlets. Estimates for sales returns are based on a variety of factors including actual returns based on expected return data communicated to it by customers. Accordingly, American Apparel believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates. At September 30, 2007, allowance for sales returns for AAI was $340.

As with any set of assumptions and estimates, there is a range of reasonably likely amounts that may be calculated for the company s allowance for sales returns above. However, American Apparel believes that there would be no significant difference in the amounts reported using other reasonable assumptions than what was used to arrive at the allowance. American Apparel regularly reviews the factors that influence its estimates and, if necessary, makes adjustments when it believes that actual product returns and credits may differ from established reserves. Actual experience may be significantly different than American Apparel s estimates.

Trade Receivables

Accounts receivable primarily consists of trade receivables, including amounts due from credit card companies, net of allowances. On a periodic basis, American Apparel evaluates its trade receivables and establishes an allowance for doubtful accounts based on a history of past bad debt expense, collections and current credit conditions. Accounts receivable primarily consists of trade receivables, including amounts due from credit card companies, net of allowances. Amounts due from credit card, debit card and electronic benefit transfer transactions as of September 30, 2007 and 2006 were approximately $1,920 and $1,117, respectively.

American Apparel performs on-going credit evaluations of its customers and adjusts credit limits based upon payment history and the customer s current credit worthiness, as determined by the review of their current credit information. Collections and payments from customers are continuously monitored. American Apparel maintains an allowance for doubtful accounts, which is based upon historical experience as well as specific customer collection issues that have been identified. While such bad debt expenses have historically been within expectations and allowances established, American Apparel cannot guarantee that it will continue to experience the same credit loss rates that it has in the past. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Inventories

Inventories are stated at the lower of cost or market. Cost is primarily determined on the first-in, first-out (FIFO) method. AAI identifies potentially excess and slow-moving inventories by evaluating turn rates, inventory levels and other factors. Excess quantities are identified through evaluation of inventory aging, review of inventory turns and historical sales experiences. At times however, AAI will purposefully engage in inventory build up at a rate that outpaces sales. This is typically done during the first quarter in anticipation of peak selling season which occurs during the summer months of the second and third quarter of the year. At such times, AAI will consider the timing of inventory buildup in order to determine whether the buildup warrants additional reserves for inventory obsolescence. If the inventory buildup precedes the selling season, management maintains the existing provision for inventory obsolescence until the peak selling season has passed and the accumulated sales data provide a better basis for an update of management s estimate of this provision. AAI has evaluated the current level of inventories considering historical sales and other factors and, based on this evaluation, has

recorded adjustments to cost of goods sold to adjust inventories to net realizable value. These adjustments are estimates, which could vary significantly, either favorably or unfavorably, from actual requirements if future economic conditions, customer demand or competition differ from expectations.

Goodwill and Other Intangible Assets

Goodwill and other intangible assets acquired in a business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142, Goodwill and Other Intangible Assets (SFAS 142). The SFAS 142 goodwill impairment model is a two-step process. The first step compares the fair value of a reporting unit that has goodwill assigned to its carrying value. American Apparel estimates the fair value of a reporting unit by using a discounted cash flow model. If the fair value of the reporting unit is determined to be less than its carrying value, a second step is performed to compute the amount of goodwill impairment, if any. Step two allocates the fair value of the reporting unit to the reporting unit s net assets other than goodwill. The excess of the fair value of the reporting unit over the amounts assigned to its net assets other than goodwill is considered the implied fair value of the reporting unit s goodwill. The implied fair value of the reporting unit s goodwill is then compared to the carrying value of its goodwill. Any shortfall represents the amount of goodwill impairment.

Long-Lived Assets

American Apparel periodically reviews the values assigned to long-lived assets, such as property, plant and equipment, intangibles and goodwill. The associated depreciation and amortization periods are reviewed on an annual basis.

Impairment of Long-Lived Assets

American Apparel follows the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 requires evaluation of the need for an impairment charge relating to long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The estimated future undiscounted cash flows associated with the asset would be compared to the asset s carrying amount to determine if a write down to a new depreciable basis is required. If required, an impairment charge is recorded based on an estimate of future discounted cash flows.

American Apparel considers the following to be some examples of important indicators that may trigger an impairment review: (i) significant under-performance or loss of key contracts acquired in an acquisition relative to expected historical or projected future operating results; (ii) significant changes in the manner or use of the acquired assets or in American Apparel s overall strategy with respect to the manner or use of the acquired assets or changes in American Apparel s overall business strategy; (iii) significant negative industry or economic trends; (iv) increased competitive pressures; (v) a significant decline in American Apparel s stock price for a sustained period of time; and (vi) regulatory changes.

American Apparel periodically evaluates acquired businesses for potential impairment indicators. Judgment regarding the existence of impairment indicators is based on market conditions and operational performance of the acquired businesses. Future events could cause American Apparel to conclude that impairment indicators exist, and therefore that goodwill and other intangible assets as well as other long lived assets are impaired. Such evaluations for impairment are significantly impacted by estimates of future revenues, costs and expenses and other factors. A significant change in cash flows in the future could result in an impairment of long lived assets.

Foreign Currency

In preparing the consolidated financial statements, the financial statements of the foreign subsidiaries are translated from the functional currency, generally the local currency, into U.S. Dollars. This process results in exchange rate gains and losses, which, under the relevant accounting guidance, are included as a separate component of stockholders equity under the caption Accumulated other comprehensive income.

Under the relevant accounting guidance, the functional currency of each foreign subsidiary is determined based on management s judgment and involves consideration of all relevant economic facts and circumstances affecting the subsidiary. Generally, the currency in which the subsidiary transacts a majority of its transactions, including billings, financing, payroll and other expenditures, would be considered the functional currency, but any dependency upon the parent and the nature of the subsidiary s operations must also be considered.

If a subsidiary s functional currency is deemed to be the local currency, then any gain or loss associated with the translation of that subsidiary s financial statements is included in accumulated other comprehensive income. However, if the functional currency is deemed to be the U.S. Dollar, then any gain or loss associated with the remeasurement of these financial statements from the local currency to the functional currency would be included within the statement of operations. If American Apparel disposes of subsidiaries, then any cumulative translation gains or losses would be recorded into the statement of operations. If American Apparel determines that there has been a change in the functional currency of a subsidiary to the U.S. Dollar, any translation gains or losses arising after the date of change would be included within the statement of operations.

Based on an assessment of the factors discussed above, American Apparel considers the relevant subsidiary s local currency to be the functional currency for each of its foreign subsidiaries.

Income Taxes

American Apparel records the estimated future tax effects of temporary differences between the tax bases of assets and liabilities and amounts reported in the accompanying consolidated balance sheets, as well as tax credit carrybacks and carryforwards. American Apparel periodically reviews the recoverability of deferred tax assets recorded on the balance sheet and provides valuation allowances as management deems necessary. Management makes judgments as to the interpretation of the tax laws that might be challenged upon an audit and cause changes to previous estimates of tax liability. In addition, American Apparel operates within multiple taxing jurisdictions and is subject to audit in these jurisdictions. In management s opinion, adequate provisions for income taxes have been made for all years. If actual taxable income by tax jurisdiction varies from estimates, additional allowances or reversals of reserves may be necessary.

Contingencies

American Apparel is subject to proceedings, lawsuits and other claims related to various matters. American Apparel is required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. Management determines the amount of reserves needed, if any, for each individual issue based on its knowledge and experience and discussions with legal counsel. The required reserves may change in the future due to new developments in each matter, the ultimate resolution of each matter or changes in approach, such as a change in settlement strategy, in dealing with these matters. American Apparel currently does not believe that these matters will have a material adverse effect on its consolidated financial position, results of operations or cash flows.

Once the proposed acquisition is completed, American Apparel s growth strategy will be to re-accelerate the number of retail locations. While there can be no assurance, American Apparel believes that there is a significant potential to expand its retail presence, with up to 800 worldwide locations in the current store format possible. In addition, American Apparel will continue to strategically expand its wholesale business. Finally, American Apparel will also look to expand the categories of merchandise it offers, specifically for denim, sweaters and accessories. To execute this growth strategy, American Apparel will leverage American Apparel s brand awareness and its vertical manufacturing experience.

As American Apparel continues to expand through organic growth, internal initiatives and future acquisitions, it will incur additional material expenses. Two of the key areas in which such increased expenses will likely occur are cost of sales as well as new merchandise development. As previously noted, in order to grow

Table of Contents

retail sales, American Apparel will have to open new retail locations and hire additional retail personnel to service new retail stores. In order to grow the wholesale distribution channel, American Apparel will have to hire new sales personnel to service new geographic territories.

To support new merchandise development, expenses will increase as AAI designs new products in existing and new categories.

Ongoing infrastructure investment also may be required to support growth. This may include expenditures for new buildings, machinery and equipment, as well as expenditures for upgraded information systems and expenditures to enhance the management team.

To reduce the impact of additional material expenses on earnings, American Apparel will have to look for ways to improve productivity of current manufacturing operations and to enhance other operating procedures. One of the initiatives already underway in its planning stage is the implementation of an ERP system that should realize gains in operation efficiencies in a number of enterprise-wide processes including inventory and production management.

Table of Contents

American Apparel, Inc.

Condensed Consolidated Statements of Operations

For the Nine Months Ended September 30, 2007 and 2006 (unaudited)

	Nine Months Ended September 30, 2007 (Unaudited)		Nine Months Ended September 30, 2006 (Unaudited)	
Net sales	$ 254,837	100.0%	$ 196,745	100.0%
Cost of sales	119,103	46.7%	106,064	53.9%
Gross profit	135,734	53.3%	90,681	46.1%
OPERATING EXPENSES				
Selling	72,631	28.5%	52,102	26.5%
Warehouse and Distribution	4,956	1.9%	4,295	2.2%
General and Administrative	30,683	12.1%	25,991	13.2%
Operating income	27,464	10.8%	8,293	4.2%
Interest expense	12,255	4.8%	7,869	4.0%
Other (Income) Expense	(1,097)	(0.4)%	(350)	(0.2)%
INCOME BEFORE INCOME TAXES	16,306	6.4%	774	0.4%
Income tax provision	4,725	1.9%	959	0.5%
NET INCOME (Loss)	$ 11,581	4.5%	$ (185)	(0.1)%

The following tables set forth AAI s net sales for the nine month period ended September 30, 2007 as compared to September 30, 2006 and provides key breakdowns within each segment of significant net sales growth from period to period. One significant factor contributing to the overall growth in net sales period to period was the expansion of our international operations, as evidenced by the opening of 14 retail stores during the nine months ended September 30, 2007. Additionally, during the same period 4 retail stores were opened and one store was closed in the United States. Also of primary significance to the expansion of AAI s retail business in the United States was AAI s increased focus on building brand awareness and targeted advertising campaigns as further described below.

	Nine Months Ended September 30, 2007		Nine Months Ended September 30, 2006			
	Amount	%	Amount	%	$ Change	% Change
NET SALES	$ 254,837	100.0%	$ 196,745	100.0%	$ 58,092	29.5%
US Wholesale	115,683	45.4%	105,330	53.5%	10,353	9.8%
US Retail	80,411	31.5%	58,008	29.5%	22,403	38.6%
International	58,743	23.1%	33,407	17.0%	25,336	75.8%
	$ 254,837	100.0%	$ 196,745	100.0%	$ 58,092	29.5%

US Wholesale: Net sales for AAI s US wholesale segment increased $10,353, an increase of 9.8%, in the nine month period ended September 30, 2007 as compared to the nine-month period ended September 30, 2006, primarily as a result of an increase in online sales due to strategic advertising and increased brand recognition as well as a result of organic growth of the wholesale business while maintaining focus on continued relationships with a set of established wholesale trading partners. One of the primary drivers behind the increase in US Wholesale sales, was the ability to meet customer demands through increased stock of inventory on hand. During the first three quarters of 2007, compared

to the first three quarters of 2006, AAI went through a phase of increased production in order to meet customer demand during the peak sales season. Online sales increased from $6,310 to $10,891, an increase of $4,581. Wholesale sales increased from $99,020 to $104,792 an increase of $5,772.

161

Table of Contents

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
US WHOLESALE BREAKDOWN:				
US - Wholesale	$ 104,792	$ 99,020	$ 5,772	5.8%
US - Online	10,891	6,310	4,581	72.6%
	$ 115,683	$ 105,330	$ 10,353	9.8%

US Retail: Net sales for the US retail store segment increased $22,403, or 38.6%, from the nine-month period ended September 30, 2006 to the comparable 2007 period, fueled by the addition of retail outlets in key markets within the US, as well as a significant increase in same store sales of 18.2%. Same-store sales are calculated as the sales increase over the previous year for stores that have been open for more than twelve months. Same-store sales contributed approximately $9,785 to the increase in US retail sales while sales from new stores contributed an additional $12,618 to the increase in US retail sales. For the nine-month period ended September 30, 2007, the average number of open stores during the period was 94 while for the nine-month period ended September 30, 2006 average number of open stores during the period was 77.

International: Net sales for AAI s International business segment increased $25,336 or 75.8% in the nine-month period ended September 30, 2007 as compared to the nine-month period ended September 30, 2006. This increase was primarily due to the increase in the number of international stores opened from 28 to 44 and partially due to the increase in same store sales of 36.4%. In the nine-month period ended September 30, 2007, AAI opened six additional stores in Germany, two in the United Kingdom, and one in each France, Italy, Japan, Korea, Netherlands and Sweden. During the period existing store sales increased from $22,834 to $31,155 or 36.4%, while sales from new stores contributed an additional $14,397 and sales from wholesale and online increased by additional $6,936. During the nine months ended September 20, 2007 approximately $9,102 and $4,089 of the international sales were generated by wholesale and online sales, respectively.

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
INTERNATIONAL BREAKDOWN:				
Retail	$ 45,552	$ 27,152	$ 18,400	67.8%
Wholesale	9,102	4,337	4,765	109.9%
Online	4,089	1,918	2,171	113.2%
	$ 58,743	$ 33,407	$ 25,336	75.8%

Cost of Sales. Cost of sales for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 is as follows:

	Nine Months Ended September 30, 2007		Nine Months Ended September 30, 2006	
	Amount	%	Amount	%
Net sales	$ 254,837	100.0%	$ 196,745	100.0%
Cost of sales	119,103	46.7%	106,064	53.9%
Gross profit	$ 135,734	53.3%	$ 90,681	46.1%

Cost of sales decreased as a percentage of net sales from 53.9% in the nine months ended September 30, 2006 to 46.7% in the nine months ended September 30, 2007. Decrease in cost of sales as a percentage of net sales was primarily related to the increase in the number of retail locations opened during 2007 and the underlying higher margin of gross profit that was realized in the retail as opposed to the wholesale channel. Decrease in the cost of sales is also a result of better operational efficiencies realized through production during

162

Table of Contents

the nine months ended September 30, 2007. During that period AAI was operating closer to its normal production capacity and was therefore able to absorb higher amounts of overhead costs into inventory costs rather than recognize these costs as period costs. A portion of the cost of sales decrease, as a % of net sales also relates to the fact that as of September 30, 2006, AAI had to increase its provision for slow-moving inventory due to inventory obsolescence concerns. This provision amounted to a cost of approximately $1,161 and accounted for approximately 1% of the net sales for the period.

Gross Profit. The following table sets forth AAI s gross profit as a percentage of net sales by segment for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006. The overall increase in the gross profit percentage for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 is a result of better efficiency in the US wholesale segment as AAI was manufacturing close to normal capacity, as well as the product mix (higher retail sales) in the total sales. This increase in gross profit is a result of an increased amount of sales being generated from US Retail, International as well as a portion of US Wholesale segment related to the online sales. Increase in international gross profit is a result of growth in international online sales and the addition of new retail stores which generate higher margins. A higher percentage of sales from retail sales and online sales generate higher margins through a lower cost of sales percentage.

	Nine Months Ended September 30, 2007 %	Nine Months Ended September 30, 2006 %	% Change
US Wholesale	27.9%	23.3%	4.6%
US Retail	77.6%	77.7%	(0.1)%
International	70.0%	62.9%	7.1%
Total	53.3%	46.1%	7.2%

Selling. Selling expenses by segment, together with unallocated corporate selling, advertising and promotion expenses, for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 increased an aggregate of 39.4%, as set forth in table below. These expenses represented 28.5% and 26.5%, respectively of the total net sales for the periods.

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
US Wholesale	$ 10,466	$ 7,393	$ 3,073	41.6%
US Retail	38,816	31,621	7,195	22.8%
International	23,349	13,088	10,261	78.4%
	$ 72,631	$ 52,102	$ 20,529	39.4%

Increases in selling expenses are primarily due to the increase in total retail stores (from 118 to 140), both in the U.S. and internationally, as well as, the strategic promotional advertising of the Company s brands and product styles throughout all of its segments. Selling expenses by type for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 are as follows:

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
SELLING:				
Advertising & catalogs	$ 8,177	$ 4,686	$ 3,491	74.5%
Payroll & fringes	32,791	23,577	9,214	39.1%

Rent, utilities, store maintenance & supplies	26,957	20,858	6,099	29.2%
Tradeshows, travel, promotions	3,232	2,613	619	23.7%
Other	1,474	368	1,106	300.5%
Total	$ 72,631	$ 52,102	$ 20,529	39.4%

163

Table of Contents

The net increase in selling expense is attributable to the following: Advertising & catalogs costs increased mainly due to the promotions for new store openings, as well as, the strategic promotional advertising of the Company s brands and product styles, AAI boosted advertising efforts through print ads, magazines and online media. Payroll costs increased as a result of increased staffing levels to support new store openings. Opened stores increased from 118 to 140. Rents, utilities, store maintenance & store supplies, travel, promotions and other expenses also increased due to company expansion driven by new store openings and as a result of new Lease Agreements entered into for new stores. Tradeshow expenses increased as a result of the additional emphasis on marketing efforts for the brand.

Warehouse and Distribution. Warehouse and distribution expenses by segment, for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 are set forth in the following table. These expenses represented 1.9% and 2.2%, respectively of the total net sales for the periods. Increase in International warehouse and distribution expenses is primarily due to an increase in transportation costs (such as import fees, duties and carrier costs) to distribute the merchandise to international subsidiaries and the increase also related to an increased number of international locations where merchandise is shipped.

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
US Wholesale	$ 4,173	$ 3,854	$ 319	8.3%
International	783	441	342	77.6%
	$ 4,956	$ 4,295	$ 661	15.4%

Warehouse and distribution expenses by type for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 are as follows:

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
WAREHOUSE AND DISTRIBUTION:				
Payroll & fringes	$ 3,760	$ 3,716	$ 44	1.2%
Other	1,196	579	617	106.6%
Total	$ 4,956	$ 4,295	$ 661	15.4%

The net increase in warehouse and distribution expense is attributable to increase in staffing necessary to support increased volume and sales growth in wholesale sales, as well as to the increase in the international distribution expenses described above.

General and Administrative. General and administrative expenses by segment, together with unallocated corporate general and administrative expenses, for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 are set forth in the following table. These expenses represented 12.1% and 13.2%, respectively of the total net sales for the periods.

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
US Wholesale	$ 2,748	$ 2,102	$ 646	30.7%
US Retail	7,150	5,018	2,132	42.5%
International	5,284	4,287	997	23.3%
Corporate	15,501	14,584	917	6.3%

	$	30,683	$	25,991	$ 4,692	18.1%

164

Table of Contents

US Wholesale segment s general and administrative expenses increased primarily due to higher levels of staffing necessary to support the expansion of AAI. The US Retail segment s general and administrative expenses increased primarily due to the increase in administrative staff to support new retail stores. Specific increased expense items include credit card fees, depreciation and amortization, and payroll. The increase in the International segment s general and administrative expenses was likewise primarily due to the additional staffing and administrative structure required to support a higher number of retail locations. Specific increased expense items include depreciation and amortization, payroll and rents. Unallocated corporate expenses increased primarily due to expenses incurred for professional service fees related to the proposed business combination with Endeavor. The increase in unallocated corporate expenses was also due to increased administrative staffing required to support the growth of the Company and provide support structure for AAI after the combination with Endeavor. Unallocated corporate expenses mainly include, professional services, consulting fees, information systems, insurance, legal and financial services provided by the corporate headquarters in Los Angeles.

General and administrative expenses by type for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 are as follows:

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change	% Change
GENERAL AND ADMINISTRATIVE:				
Payroll & fringes	$ 9,161	$ 7,731	$ 1,430	18.5%
Rent, utilities, maintenance	2,597	1,938	659	34.0%
Depreciation & amortization	6,047	5,288	759	14.4%
Professional fees	5,615	4,366	1,249	28.6%
Credit card fees	2,432	2,181	251	11.5%
Other	4,831	4,487	344	7.7%
Total	$ 30,683	$ 25,991	$ 4,692	18.1%

The net increase in general and administrative expense is attributable to the following: Payroll costs increased mainly due to the increase in retail store locations and increased wholesale sales growth and the related general salary increases, which increased mainly due to the increase in number of open retail stores. Depreciation and amortization costs increases, due to buildouts of leasehold improvements and additions of machinery and information systems equipment required to support the growth in wholesale, retail and online distribution channels. Professional fees increased due to additional costs incurred in the proposed business combination with Endeavor.

Interest Expenses. The major components of interest expense are interest on the outstanding revolving credit facility, loans from related and unrelated parties and term loan for a private investment firm. AAI increased its levels of debt primarily in order to finance its expansion and buildout of retail stores opened during the period. Financing was also used to purchase additional manufacturing and information systems equipment required to support higher manufacturing throughout required to support increased sales in all segments. Interest rates on debt ranged from 4.6% to 24% during the nine-month period ended September 30, 2007. Interest expense for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 were $12,255 and $7,869, respectively. These expenses represented 4.8% and 4.0%, respectively, of the total net sales for the periods. The net increase in interest expense is attributable to the increase in interest bearing debt. There was no significant change in the effective interest rate. Total interest bearing debt increased from $86,337 to $119,622.

Table of Contents

Other (Income) Expense, Net. Other (income) expense, net for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 are set forth in the following table. These expenses represented (0.4)% and (0.2)%, respectively, of the total net sales for the periods.

	Nine Months Ended September 30, 2007 Amount	Nine Months Ended September 30, 2006 Amount	$ Change
OTHER (INCOME) EXPENSE:			
Foreign currency transaction gain	$ (20)	$ (436)	$ 416
Other (income) expense	(1,077)	86	(1,163)
	$ (1,097)	$ (350)	(747)

The decrease in other (income) expense, is primarily due to recovery on certain insurance claims as well as proceeds from an implementation of a environmentally-friendly waste recycling program.

Income Taxes. Income tax provision increased from approximately $959 for the nine months ended September 30, 2006 to approximately $4,725 for the nine months ended September 30, 2007, as a result of an increase in foreign taxable income. AAI is a subchapter S corporation, therefore, domestic earnings and losses for Federal tax reporting purposes are included in the personal tax returns of the stockholders and taxed according to their personal tax strategies. Accordingly, AAI does not incur additional Federal income tax obligations, and the consolidated financial statements do not include any provision for Federal income taxes. Where applicable, state income taxes are provided by AAI at the applicable statutory rates multiplied by pre-tax income. AAI files income tax returns in various states. Some of these states accept subchapter S corporation status, while in some states AAI is taxed at C corporation tax rates and in the remaining states, it is taxed at reduced rates applicable to S corporations.

Net Income (Loss). AAI s net income (loss) after income taxes for the nine months ended September 30, 2007 as compared to the nine months ended September 30, 2006 were $11,581 and $(185), respectively. A significant factor contributing to the increase in AAI s net income after income taxes from period to period was a significant increase in net sales, combined with the reduction in cost of sales as a percentage of net sales as well as higher operating income as a percentage of net sales.

166

American Apparel, Inc.

Consolidated Statements of Operations

For the Twelve Months Ending December 31, 2006 and 2005

	Twelve Months Ended December 31, 2006		Twelve Months Ended December 31, 2005	
Net sales	$ 264,691	100.0%	$ 188,106	100.0%
Cost of sales	138,385	52.3%	101,048	53.7%
Gross profit	126,306	47.7%	87,058	46.3%
OPERATING EXPENSES				
Selling	73,506	27.8%	45,767	24.3%
Warehouse and Distribution	6,681	2.5%	4,160	2.2%
General and Administrative	36,819	13.9%	26,896	14.4%
Operating income	9,300	3.5%	10,235	5.4%
Interest expense	10,797	4.1%	6,258	3.3%
Other (Income) Expense	(1,208)	(0.5)%	2	0.0%
(LOSS) INCOME BEFORE INCOME TAXES	(289)	(0.1)%	3,975	2.1%
Income tax provision	1,335	0.5%	392	0.2%
NET (LOSS) INCOME	$ (1,624)	(0.6)%	$ 3,583	1.9%

Net Sales. The following table sets forth AAI s net sales for the for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 and provides key breakdowns within each segment of significant net sales growth from period to period. Net sales were as follows:

	Twelve Months Ended December 31, 2006		Twelve Months Ended December 31, 2005			
	Amount	%	Amount	%	$ Change	% Change
NET SALES	$ 264,691	100.0%	$ 188,106	100.0%	$ 76,585	40.7%
US Wholesale	138,056	52.2%	128,274	68.2%	9,782	7.6%
US Retail	80,210	30.3%	45,532	24.2%	34,678	76.2%
International	46,425	17.5%	14,300	7.6%	32,125	224.7%
	$ 264,691	100.0%	$ 188,106	100.0%	$ 76,585	40.7%

Net sales increased $76,585 or 40.7% from approximately $188,106 in the twelve months ended December 31, 2005 to approximately $264,691 for the twelve months ended December 31, 2006. This sales increase was primarily attributable to opening 41 new retail locations while closing 2 existing locations during 2006. The number of retail locations in the United States increased from 66 as of December 31, 2005 to 93 as of December 31, 2006. The number of international retail locations increased from 18 as of December 31, 2005 to 30 as of December 31, 2006.

Table of Contents

US Wholesale. Net sales for the US wholesale segment increased $9,782 or 7.6% from approximately $128,274 in the twelve months ended December 31, 2005 to approximately $138,056 for the twelve months ended December 31, 2006. This increase is a result of increased wholesale sales of $6,124 or 5.0% and increased US online sales of $3,658 or 68.1%. We believe the online sales segment will continue to grow as a percentage of our total annual net sales in the future. Online sales generally have a much higher gross margin than our traditional wholesale sales. US wholesale sales for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 is as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
US WHOLESALE BREAKDOWN				
US Wholesale	$ 129,024	$ 122,900	$ 6,124	5.0%
US Online	9,032	5,374	3,658	68.1%
	$ 138,056	$ 128,274	$ 9,782	7.6%

US Retail. Net sales for the US retail store segment increased $34,678 or 76.2%, for the twelve months ended December 31, 2006 to the comparable 2005 period, fueled by the addition of retail outlets in key markets within the US. New store sales contributed approximately $36,279 to the increase in US retail sales offset by a slight decrease in same store sales of $1,601. For the twelve months ended December 31, 2006, average number of open stores during the period was 81 while for the twelve months ended December 31, 2005, average number of open stores during the period was 44.

International: Net sales for International segment increased $32,125 or 224.7% for the twelve months ended December 31, 2006 to the comparable 2005 period. This increase was primarily due to the number of international stores opened during the year and partially due to the increase in same store sales. New store sales contributed approximately $23,422 to the increase in International sales, same store sales contributed approximately $3,804 and wholesale & online sales contributed approximately $4,899. For the twelve months ended December 31, 2006, average number of open stores during the period was 25 while for the twelve months ended December 31, 2005, average number of open stores during the period was 9.

	Twelve Months Ended December 31,			
	2006 Amount	2005 Amount	$ Change	% Change
INTERNATIONAL BREAKDOWN				
Retail	$ 37,816	10,590	27,226	257.1%
Wholesale	5,762	3,399	2,363	69.5%
Online	2,847	311	2,536	815.4%
	$ 46,425	14,300	32,125	224.7%

Cost of Sales. Cost of sales increased from approximately $101,048 for the twelve months ended December 31, 2005 to approximately $138,385 for the twelve months ended December 31, 2006. Cost of sales decreased as a percentage of net sales from 53.7% in the twelve months ended December 31, 2005 to 52.3% in the twelve months ended December 31, 2006. The decrease in cost of sales as a percentage of net sales is primarily related to a shift in American Apparel s sales mix. Cost of sales for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 is as follows:

	Twelve Months Ended December 31, 2006		Twelve Months Ended December 31, 2005	
	Amount	%	Amount	%
Net sales	$ 264,691	100.0%	$ 188,106	100.0%

Cost of sales	138,385	52.3%	101,048	53.7%
Gross profit	$ 126,306	47.7%	$ 87,058	46.3%

168

Table of Contents

The decrease in cost of sales as a percentage of net sales of 1.4% was caused by AAI s sales mix. A higher percentage of our sales were from retail sales with a lower cost of sales percentage as compared to wholesale sales. The overall decrease was partially offset by an increase in the inventory reserve and unabsorbed overhead. During 2005 and the first half of 2006, AAI increased production of certain styles and introduced certain new styles which would be needed to support the anticipated further expansion into the retail channel in 2006. Due to the changing sales mix in 2006 and the increase in retail sales, AAI s growth in overall sales volume was substantially faster than the growth in the number of units sold. However, while evaluating the inventory obsolescence reserves for 2006, it became evident that certain styles did not achieve expected sales levels. As a matter of policy, AAI keeps stock of a wide variety of styles, sizes and colors in order to keep commitments to customers and be responsive to customer needs.

Nevertheless, in the later part of 2006 AAI considered the possibility of having an excess of certain styles on hand. As there is no assurance that demands for these styles will materialize, AAI increased its reserve for slow-moving inventory from $800 as of December 31 2005 to $4,284 as of December 31, 2006. The overall decrease in cost of sales as a percentage of sales was also offset by costs not absorbed by production caused by financing constraints in the fourth quarter of fiscal 2006 as well as the increased costs resulting from rapid introduction of multiple new styles for the retail channel. Gross profit increased as a percentage of sales, from 46.3% for the twelve months ended December 31, 2005 to 47.7% for the twelve months ended December 31, 2006.

Gross Profit. The overall increase in the gross profit percentage for the twelve months ended December 31, 2006, as compared to the twelve months ended December 31, 2005 is a result of the change in sales mix. A higher percentage of our sales are coming from retail sales at a higher gross margin. American Apparel s US Retail and International segments (domestic and foreign) have generated an increased percentage of net sales during 2006 as compared to 2005. American Apparel s US Retail and International segments have higher gross margins as compared to its US Wholesale segment. Gross profit as a percentage of net sales by segment for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 is as follows:

	Twelve Months Ended December 31, 2006 %	Twelve Months Ended December 31, 2005 %	% Change
US Wholesale	22.9%	31.0%	(8.1)%
US Retail	78.5%	82.5%	(4.0)%
International	68.3%	67.9%	0.4%
Total	47.7%	46.3%	1.4%

The US wholesale decrease in the gross profit percentage for the year ended December 31, 2006 as compared to year ended December 31, 2005 is a result of an increase to the reserve for slow-moving inventory of $3,484 Representing 2.5% of the decrease. In addition, the decrease in gross profit was also a result of a slowdown in production in the last quarter of 2006. As a result of a slowdown in production, a lower amount of overhead was absorbed into inventory and a significant amount of overhead was recognized as a component of cost of sales in that period. Consequently, US wholesale gross profit was reduced from 31.0% to 22.9%.

US Retail gross profit decreased from 82.5% for the twelve months ended December 31, 2005 to 78.5% for the twelve months ended December 31, 2006. This decrease is primarily caused by the purchasing price from the US wholesale segment. During 2006, US wholesale costs increased and these increased costs were passed on to the US Retail segment. The increased costs were primarily caused by the higher fabric and yarn costs.

International gross profit increased from 67.9% for the twelve months ended December 31, 2005 to 68.3% for the twelve months ended December 31, 2006. This increase is primarily caused by the sales product mix. A higher percentage of sales from retail and online sales generate a higher gross profit margin through a lower cost of sales percentage as compared to wholesale sales.

Table of Contents

Selling. Selling, expenses by segment together with unallocated corporate selling, advertising and promotion expenses, for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
US Wholesale	$ 9,789	$ 11,819	$ (2,030)	(17.2)%
US Retail	44,561	26,265	18,296	69.7%
International	19,156	7,683	11,473	149.3%
	$ 73,506	$ 45,767	$ 27,739	60.6%

Selling, expenses increased $27,739 or 60.6% from approximately $45,767 for the twelve months ended December 31, 2005 to approximately $73,506 for the twelve months ended December 31, 2006. Increases in selling, advertising and promotions are primarily due to the increase in total retail stores from 84 to 123, as well as, the strategic promotional advertising of the AAI s brands and product styles.

Selling, advertising and promotional expenses by type for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
SELLING:				
Advertising & catalogs	$ 7,138	$ 5,732	$ 1,406	24.5%
Payroll & fringes	32,751	18,851	13,900	73.7%
Rent, utilities, store maintenance & supplies	28,442	16,439	12,003	73.0%
Tradeshows, travel, promotions	3,329	3,224	105	3.3%
Other	1,846	1,521	325	21.4%
Total	$ 73,506	$ 45,767	$ 27,739	60.6%

The net increase in selling expense is attributable to the following: Advertising & catalogs costs increased mainly due to the promotions for new store openings. AAI increased advertising efforts through print ads, magazines and online media. Payroll costs increased as a result of increased staffing levels to support new store openings. Opened stores increased from 84 to 123. Rents, utilities, store maintenance & store supplies increased due to new store openings. Other expenses increased due to new store openings and the increase in overall sales.

Warehouse and Distribution. Warehouse and distribution expenses by segment, for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
US - Wholesale	$ 5,027	$ 3,236	$ 1,791	55.3%
International	1,654	924	730	79.0%
	$ 6,681	$ 4,160	$ 2,521	60.6%

Warehouse and distribution expenses increased $2,521 or 60.6% from approximately $4,160 for the twelve months ended December 31, 2005 to approximately $6,681 for the twelve months ended December 31, 2006. As

170

Table of Contents

a percentage of net sales this increase represented an increase from 2.2% of net sales to 2.5% of net sales. This increase is primarily related to additional salaries and costs after another warehouse building was occupied during 2006. Increase in International expenses is primarily due to increase in transportation costs, such as, import fees, duties and carrier costs, to additional locations.

Warehouse and distribution expenses by type for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
WAREHOUSE AND DISTRIBUTION				
Payroll & fringes	$ 4,823	$ 3,198	$ 1,625	50.8%
Other	1,858	962	896	93.1%
Total	$ 6,681	$ 4,160	$ 2,521	60.6%

General and Administrative. General and administrative expenses by segment, together with unallocated corporate general and administrative expenses, for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are set forth in the following table. These expenses represented 13.9% and 14.3%, respectively of the total net sales for the periods.

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
US - Wholesale	$ 2,597	$ 2,485	$ 112	4.5%
US - Retail	6,897	4,552	2,345	51.5%
International	6,174	1,986	4,188	210.9%
Corporate	21,151	17,873	3,278	18.3%
	$ 36,819	$ 26,896	$ 9,923	36.9%

Increase in US Wholesale segment s general and administrative expenses are primarily due to higher levels of staffing necessary to support the expansion of AAI. The US Retail segment s general and administrative expenses increased primarily due to the increase in administrative staff to support new retail stores. Specific increased expense items include credit card fees, depreciation and amortization and payroll. The International segments general and administrative expenses increase was likewise primarily due to the additional staffing and administrative structure required to support a higher number of retail locations. Specific increased expense items include depreciation and amortization and payroll. Unallocated corporate expenses increased primarily due to expenses incurred for professional service fees related to the proposed business combination with Endeavor. As well as, increased administrative staffing required to support the growth of AAI and provide support structure for AAI after the combination with Endeavor.

General and administrative expenses by type for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change	% Change
GENERAL AND ADMINISTRATIVE				
Payroll & fringes	$ 10,695	$ 8,519	$ 2,176	25.5%
Rent, utilities, maintenance	3,712	3,158	554	17.5%
Depreciation & amortization & impairment	7,281	3,735	3,546	94.9%
Professional fees	6,838	5,171	1,667	32.2%

Credit card fees		3,027		1,155	1,872	162.1%
Bad debts		1,121		576	545	94.6%
Other		4,145		4,582	(437)	-9.5%
Total	$	36,819	$	26,896	$ 9,923	36.9%

171

Table of Contents

The net increase in general and administrative expenses in attributable to the following: Payroll costs increased mainly due to the increase in retail and wholesale sales growth and general salary increases. Rent, utilities & maintenance costs increased mainly due to the additional space used by wholesale. Depreciation and amortization costs increased due to build outs or leasehold improvements and additions to support the growth in wholesale and retail. Professional fees increased due to additional costs incurred in the accounting and legal areas, Credit card fees increased due to increase in sales volume for both retail and wholesale and bad debts increased mainly due to the increase in the wholesale segment.

Interest Expenses. The major components of interest expense are interest on the outstanding revolving credit facility, term loans with banks, loans from related and unrelated parties. Interest expense for the year ended December 31, 2006 as compared to the year ended December 31, 2005 is as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change
INTEREST EXPENSE	$ 10,797	$ 6,258	$ 4,539

Interest expense increased $4,539 or 72.5% from approximately $6,258 for the twelve months ended December 31, 2005 to approximately $10,797 for the twelve months ended December 31, 2006. This increase was primarily attributable to increased borrowing levels and higher interest rates in 2006 to support the rapid growth of American Apparel. Total interest bearing debt increased from $73,012 to $85,129.

Other (Income) Expense, Net. Other (income) expense, net for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change
OTHER (INCOME) EXPENSE			
Foreign currency transaction (gain) loss	$ (601)	$ 358	$ (959)
Other income	(607)	(356)	(251)
	$ (1,208)	$ 2	$ (1,210)

The increase in other (income) expense, net is primarily due to the foreign exchange transaction (gain) associated with the weakening of the U.S. Dollar against the foreign currency as compared to the prior comparable period.

Income Taxes. Income tax expense for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 are as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change
PROVISION FOR INCOME TAXES	$ 1,335	$ 392	$ 943

Income tax provision increased from approximately $392 for the twelve months ended December 31, 2005 to approximately $1,335 for the twelve months ended December 31, 2006, as a result of an increase in foreign taxable income. AAI is a subchapter S corporation. Therefore, domestic earnings and losses for Federal tax reporting purposes are included in the personal tax returns of the stockholders and taxed according to their personal tax strategies. Accordingly, AAI does not incur additional Federal income tax obligations, and the consolidated financial statements do not include any provision for Federal income taxes. Where applicable, state income taxes are provided by AAI at the applicable statutory rates multiplied by pre-tax income. AAI files

172

Table of Contents

income tax returns in various states. Some of these states accept subchapter S corporation status, while in some states AAI is taxed at C corporation tax rates and in the remaining states; it is taxed at reduced rates applicable to S corporations.

Net (Loss) Income. Net (Loss) income for the twelve months ended December 31, 2006 as compared to the twelve months ended December 31, 2005 is as follows:

	Twelve Months Ended December 31, 2006 Amount	Twelve Months Ended December 31, 2005 Amount	$ Change
NET (LOSS) INCOME	$ (1,624)	$ 3,583	$ (5,207)

Net income decreased from approximately $3,583 for the twelve months ended December 31, 2005 to a loss of approximately $1,624 for the twelve months ended December 31, 2006. This decrease was primarily attributable to the increase in selling, general and administrative and interest expense as described above.

173

American Apparel, Inc.

Condensed Consolidated Statements of Operations

For the Twelve Months Ended December 31, 2005 and 2004 (unaudited)

	Twelve Months Ended December 31, 2005		Twelve Months Ended December 31, 2004 (Unaudited)	
Net sales	$ 188,106	100.0%	$ 127,929	100.0%
Cost of sales	101,048	53.7%	80,995	63.3%
Gross profit	87,058	46.3%	46,934	36.7%
OPERATING EXPENSES				
Selling	45,767	24.3%	19,547	15.3%
Warehouse and Distribution	4,160	2.2%	4,061	3.2%
General and Administrative	26,896	14.4%	14,068	11.0%
Operating income	10,235	5.4%	9,258	7.2%
Interest expense	6,258	3.3%	1,928	1.5%
Other (Income) Expense	2	0.0%	(12)	0.0%
INCOME BEFORE INCOME TAXES	3,975	2.1	7,342	5.7%
Income tax provision	392	0.2	1,019	0.8%
NET INCOME	$ 3,583	1.9%	$ 6,323	4.9%

Net Sales: Net sales increased $60,177 or 47.0% from approximately $127,929 in the twelve months ended December 31, 2004 to approximately $188,106 for the twelve months ended December 31, 2005. This sales increase was primarily attributable to the opening of 55 new retail locations worldwide during 2005. The number of retail locations in the United States increased from 26 as of December 31, 2004 to 66 as of December 31, 2005. The number of international retail locations increased from 3 as of December 31, 2004 to 18 as of December 31, 2005.

The following table sets forth AAI s net sales for the twelve month period ended December 31, 2005 as compared to December 31, 2004 and provide key breakdowns within each segment of significant net sales growth from period to period.

	Twelve Months Ended December 31, 2005		Twelve Months Ended December 31, 2004			
	Amount	%	Amount	%	$ Change	% Change
NET SALES	$ 188,106	100.0%	$ 127,929	100.0%	$ 60,177	47.0%
US Wholesale	128,274	68.2%	117,716	92.0%	10,558	9.0%
US Retail	45,532	24.2%	7,810	6.1%	37,722	483.0%
International	14,300	7.6%	2,403	1.9%	11,897	495.1%
	$ 188,106	100.0%	$ 127,929	100.0%	60,177	47.0%

US Wholesale: Net sales for AAI s US wholesale segment increased $10,558, an increase of 9.0%, in the twelve month period ended December 31, 2005 as compared to the twelve-month period ended December 31, 2004. This increase was primarily as a result of increase in

wholesale sales, which accounted for 94.8% of total wholesale sales and increase in online sales, a component of US Wholesale, which represented 5.2% of the total wholesale sales for 2005. Growth in US wholesale segment was driven by increased customer demand as well as strategic advertising for both wholesale and online service channels.

US Retail: Net sales for the US retail store segment increased $37,722 or 483.0%, to $45,532 from $7,810 for the twelve months ended December 31, 2005 compared to the twelve month period ended December 31, 2004. This increase is partially due to the increase in stores from 26 to 66 and partially due to increases in same

174

Table of Contents

store sales of 45.9%. Same-store sales are calculated as the sales increase over the previous year for stores that have been open for more than twelve months. Same store sales contributed approximately $4,625 to the increase in US retail sales while sales from new stores contributed an additional $33,097 to the increase in US retail sales.

International: Net sales for the International segment increased $11,897 or 495.1%, to $14,300 from $2,403 for the twelve months ended December 31, 2005 compared to the twelve month period ended December 31, 2004. This increase is partially due to the increase in stores from 3 to 18 and partially due to increases in same store sales of 98.2%. In the twelve-month period ended December 31, 2005, AAI opened four new stores in France, three stores in Germany, three in Japan, two in Mexico, and one in each Korea, Switzerland and the United Kingdom. Same store sales contributed approximately $988 to the increase in International sales while sales from new stores contributed additional $10,908 to the increase in International sales.

Cost of Sales. Cost of sales increased from approximately $80,995 for the twelve months ended December 31, 2004 to approximately $101,048 for the twelve months ended December 31, 2005. Cost of sales decreased as a percentage of net sales from 63.3% in the twelve months ended December 31, 2004 to 53.7% in the twelve months ended December 31, 2005. The decrease in cost of sales as a percentage of sales was attributable to AAI s sales mix. A higher percentage of sales were from retail sales and online sales which generate higher margins through a lower cost of sales percentage.

The following table sets forth AAI s cost of sales for the year ended December 31, 2005 as compared to the year ended December 31, 2004.

	Twelve Months Ended December 31, 2005		Twelve Months Ended December 31, 2004	
	Amount	%	Amount	%
Net sales	$ 188,106	100.0%	$ 127,929	100.0%
Cost of sales	101,048	53.7%	80,995	63.3%
Gross profit	$ 87,058	46.3%	$ 46,934	36.7%

Gross Profit. Gross profit dollars increased from approximately $46,934 for the twelve months ended December 31, 2004 to approximately $87,058 for the twelve months ended December 31, 2005. This change was attributable to the increase in net sales as well as the change in revenue mix from AAI s business segments. Wholesale revenue increased from approximately $117,716 for the twelve months ended December 31, 2004 to approximately $128,274 for the twelve months ended December 31, 2005, an increase of 9%. In the meantime revenue from retail operations increased from approximately $7,810 for the twelve months ended December 31, 2004 to approximately $45,532 for the twelve months ended December 31,2005, an increase of approximately 483%. AAI realizes higher gross margins on its retail sales as opposed to wholesale sales. As a result, gross profit increased as a percentage of sales, from 36.7% for the twelve months ended December 31, 2004 to 46.3% for the twelve months ended December 31, 2005.

The following table sets forth AAI s gross profit as a percentage of net sales by segment for the twelve months ended December 31, 2005 as compared to the twelve months ended December 31, 2004.

	Twelve Months Ended December 31, 2005	Twelve Months Ended December 31, 2004	
	%	%	% Change
US Wholesale	31.0%	32.8%	(1.8%)
US Retail	82.5%	82.9%	(0.4%)
International	67.9%	78.4%	(10.5%)
Total	46.3%	36.7%	9.6%

Table of Contents

Selling. Selling expenses by segment, together with unallocated corporate selling, advertising and promotions expenses increased from approximately $19,547 for the twelve months ended December 31, 2004 to approximately $45,767 for the twelve months ended December 31, 2005. This increase was primarily attributable to increased rent, payroll, advertising, promotion and catalog expenses associated with opening of new retail stores, and a higher level of sales and promotional campaigns during 2005. Selling expenses also increased as a percentage of sales from 15.3% in the twelve months ended December 31, 2004 to 24.3% for the twelve months ended December 31, 2005, as AAI spent higher amounts on retail store startup costs and location advertising.

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change	% Change
US - Wholesale	$ 11,819	$ 12,049	$ (230)	(1.9)%
US - Retail	26,265	5,035	21,230	421.6%
International	7,683	2,463	5,220	211.9%
	$ 45,767	$ 19,547	$ 26,220	134.1%

The net increase in selling, advertising and promotion expense is attributable to the following: Advertising & catalogs costs increased mainly due to the promotions for new store openings, Payroll costs increased mainly due to increase in staffing required due to new store openings from 28 at December 31, 2004 to 84 as of December 31, 2005 and general salary increases, Rents, utilities store maintenance & store supplies increased mainly due to new store openings, and Other expenses increased due to new lease agreements entered into to facilitate new store openings and the increase in overall sales.

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change	% Change
SELLING:				
Advertising & catalogs	$ 5,732	$ 3,436	$ 2,296	66.8%
Payroll & fringes	18,851	8,321	10,530	126.5%
Rent, utilities, store maintenance & supplies	16,439	3,030	13,409	442.5%
Tradeshows, travel, promotions	3,224	2,548	676	26.5%
Other	1,521	2,212	(691)	(31.2)%
Total	$ 45,767	$ 19,547	$ 26,220	134.1%

Warehouse and Distribution. Warehouse and distribution expenses by segment, together with unallocated corporate warehouse and distribution expenses, increased from approximately $4,061 for the twelve months ended December 31, 2004 to approximately $4,160 for the twelve months ended December 31, 2005. As a percentage of sales this represented a drop from 3.2% of sales down to 2.2%. This decrease as a percentage of net sales was related to the fact that during 2005 AAI did not require additional warehousing capacity in order to support expansion as AAI s existing facilities were sufficient to support its then-current requirements.

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change	% Change
US - Wholesale	$ 3,236	3,608	$ (372)	(10.3)%
International	924	453	471	104.0%
	$ 4,160	$ 4,061	$ 99	2.4%

176

Table of Contents

The net increase in international warehouse and distribution expense is mainly attributable to the increase in import fees and duties as a result of higher sales volume realized overseas. Warehouse and distribution expenses by type for the twelve months ended December 31, 2005 as compared to the twelve months ended December 31, 2004 are as follows:

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change	% Change
WAREHOUSE AND DISTRIBUTION:				
Payroll & fringes	$ 3,236	$ 3,246	$ (10)	(0.3%)
Other	934	815	109	13.4%
Total	$ 4,160	$ 4,061	$ 99	2.4%

General and Administrative. General and administrative expenses by segment, together with unallocated corporate general and administrative expenses, increased from approximately $14,068 for the twelve months ended December 31, 2004 to approximately $26,896 for the twelve months ended December 31, 2005. This increase was primarily related to the increase in rent expense for leases at manufacturing facilities. In addition, other significant increases were evident in salaries and wages, depreciation and amortization, credit card service fees and utilities, all related to the buildup of staff, equipment and related information systems support structure required to support store expansion and sales increases.

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change	% Change
US - Wholesale	$ 2,485	$ 1,929	$ 556	28.8%
US - Retail	4,552	531	4,021	757.3%
International	1,986	457	1,529	334.6%
Corporate	17,873	11,151	6,722	60.3%
	$ 26,896	$ 14,068	$ 12,828	91.2%

The net increase in general and administrative expenses in attributable to the following: Payroll costs increased mainly due to the increase in administrative staff required to support retail and wholesale sales growth, rent, utilities and maintenance costs increased mainly due to purchase of a dye house lease agreement and related equipment. Depreciation and amortization costs increased due to additions in property, plant and equipment to support the growth in wholesale and retail. Professional fees increased due to additional costs incurred in the accounting and legal, Credit card fees increased due to increase in sales volume for both retail and wholesale and bad debts decreased mainly due to better collection efforts for the twelve months ended December 31, 2005.

General and administrative expenses by type for the twelve months ended December 31, 2005 as compared to the twelve months ended December 31, 2004 are as follows:

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change	% Change
GENERAL AND ADMINISTRATIVE:				
Payroll & fringes	$ 8,519	$ 3,868	$ 4,651	120.2%
Rent, utilities, maintenance	3,158	2,884	274	9.5%
Depreciation & amortization & impairment	3,735	1,392	2,343	168.3%

Professional fees		5,171		1,527	3,644	238.6%
Credit card fees		1,155		542	613	113.1%
Bad Debts		576		1,366	(790)	(57.8%)
Other		4,582		2,489	2,093	84.1%
Total	$	26,896	$	14,068	$ 12,828	91.2%

177

Table of Contents

Interest Expenses. Interest expense increased from approximately $1,928 for the twelve months ended December 31, 2004 to approximately $6,258 for the twelve months ended December 31, 2005. AAI increased its levels of debt primarily in order to finance its expansion and buildout of retail stores opened during the period. Financing was also used to purchase additional manufacturing and information systems equipment required to support higher manufacturing throughput required to support increased sales in all segments. Interest rates on debt ranged from approximately 4% to approximately 18% during the twelve-month period ended December 31, 2005. The major components of interest expense are interest on the outstanding revolving credit facility, term loans with banks, loans from related and unrelated parties. Total interest bearing debt increased from $48,595 to $73,012.

Other (Income) Expense, Net. Other (income) expense, net for the twelve months ended December 31, 2005 as compared to the twelve months ended December 31, 2004 are set forth in the following table. The decrease in other (income) expense, net is primarily due to the foreign exchange transaction loss associated with the strengthening of the U.S. Dollar against the foreign currency as compared to the prior comparable period.

	Twelve Months Ended December 31, 2005 Amount	Twelve Months Ended December 31, 2004 Amount	$ Change
OTHER (INCOME) EXPENSE:			
Foreign currency transaction loss (gain)	$ 358	$ (352)	$ 710
Other (income) expense	(356)	340	(696)
	$ 2	$ (12)	14

Income Taxes. Income tax provision decreased from approximately $1,019 for the nine months ended December 31, 2004 to approximately $392 for the twelve months ended December 31, 2005. AAI is a subchapter S corporation, therefore, domestic earnings and losses for Federal tax reporting purposes are included in the personal tax returns of the stockholders and taxed according to their personal tax strategies. Accordingly, AAI does not incur additional Federal income tax obligations, and the consolidated financial statements do not include any provision for Federal income taxes. Where applicable, state income taxes are provided by AAI at the applicable statutory rates multiplied by pre-tax income. AAI files income tax returns in various states. Some of these states accept subchapter S corporation status, while in some states AAI is taxed at C corporation tax rates and in the remaining states, it is taxed at reduced rates applicable to S corporations.

Net Income (Loss). Net income decreased from approximately $6,323 for the twelve months ended December 31, 2004 to approximately $3,583 for the twelve months ended December 31, 2005. This decrease was primarily attributable to the increase in selling, general and administrative and interest expense which where required to support the growth of AAI through 2005.

Table of Contents

The CI Companies

Condensed Combined Statements of Income

For the Nine Months Ending September 30, 2007 and 2006 (unaudited)

(in thousands CDN$)

	Nine Months Ended September 30,			
	2007 (Unaudited)		2006 (Unaudited)	
Sales	$ 33,100	100.00%	$ 25,837	100.00%
Cost of sales	12,044	36.39%	9,670	37.43%
Gross profit	21,056	63.61%	16,167	62.57%
OPERATING EXPENSES				
Selling expenses	10,004	30.22%	8,854	34.27%
Warehouse and distribution expenses	2,488	7.52%	2,143	8.29%
General and administrative expenses	5,802	17.53%	3,991	15.45%
Operating Income	2,762	8.34%	1,179	4.56%
Interest expense	991	2.99%	803	3.11%
Income before income taxes	1,771	5.35%	376	1.45%
Income-Tax Provision	812	2.45%	259	1.00%
Net income	$ 959	2.90%	$ 117	0.45%

Nine months ended September 30, 2007 compared with nine months ended September 30, 2006

Net sales for the nine months ended September 30, 2007 were approximately $33,100, a $7,263 or 28.1% increase from the sales of approximately $25,837 for the nine months ended September 30, 2006.

Retail sales for the period increased to $22,906 from $15,955. This increase of $6,951 is attributable to the increase in comparable store sales of $3,667, or 23.0% with the balance of the increase of $3,284 due to the opening of three additional stores from September to December 2006 and the closing of one existing store from January 2007 through September 2007 for a total of 25 stores as at September 30, 2007. The main contributing factor in the increase of retail sales from 2006 to 2007 is due to the greater variety of items being sold at our stores and the remerchandising of our stores to better display our products. During the period, American Apparel expanded its fabric offerings which facilitated introduction of new styles across the wholesale and retail distribution channels. As many as thirty new styles were added to the retail distribution channel of which the most notable was the addition of denim products. While many of the new accounts have placed small initial orders we feel that they provide additional basis for future growth of the wholesale segment.

Wholesale sales increased to $10,194 in 2007 from $9,881 in 2006 for a total increase of $313 or 3.1%. This increase can be attributed to our increased efforts to expand our wholesale clientele which led to opening of 442 new accounts.

Gross profit increased 30.2% from approximately $16,167 for the nine months ended September 30, 2006 to approximately $21,056 for the nine months ended September 30, 2007. Retail gross profit has increased to $17,041, or 74.4% of sales, for 2007 from $11,601, or 72.7% of sales, for 2006. The increase in our retail gross profit percentage is mainly attributable to favorable exchange rates for purchases denominated in US dollars. Wholesale gross profit decreased to $4,015, or 39.4% of sales, in 2007 from $4,565, or 46.2% of sales, in 2006. The decrease in our wholesale gross profit can be attributed mainly to lower prices which were set to increase our sales volume and remain competitive in the wholesale market. The increase in gross profit to 63.6% of sales in 2007 from 62.6% of sales in 2006 can be attributed to a greater percentage of our total sales coming from retail versus wholesale with the higher gross profit percentage earned on retail sales.

179

Table of Contents

General and administrative expenses increased to approximately $5,802 for the nine months ended September 30, 2007 from $3,991 for the same period in 2006. Retail general and administrative expenses increased to $3,676 in 2007 from $1,573 in 2006 due to an increase in management fees paid to the shareholder from $1,274 in 2006 to $2,750 in 2007. Retail professional fees increased to $601 in 2007 from $135 in 2006 mainly due to the increased reporting standards necessitated by the Endeavor transaction.

Wholesale general and administrative expenses decreased to $2,127 in 2007 from $2,418 in 2006. Wholesale management fees paid to the shareholder decreased to $250 in 2007 from $550 in 2006 while wholesale professional fees increased to $264 in 2007 from $179 in 2006 mainly due to the increased reporting standards necessitated by the Endeavor transaction

Selling expenses increased to approximately $10,004 in 2007 from $8,854 in 2006. Retail selling expenses increased to $8,961 in 2007 from $7,856 in 2006 and wholesale selling expenses increased to $1,043 from $997 during this same period. Retail salaries and wages increased to $3,370 in 2007 from $2,872 in 2006 and retail rent increased to $3,189 in 2007 from $2,750 in 2006. Both of these increases can be mainly attributed to our opening of three new stores in the last half of 2006.

Warehouse and distribution expenses increased to $2,488 in 2007 from $2,143 in 2006. Retail warehouse salaries increased from $683 in 2006 to $1,296 in 2007 due to the extra labor required for the increased sales volume in 2007 while wholesale warehouse salaries decreased to $821 in 2007 from $1,040 in 2006.

Interest expense increased from approximately $803 for the nine months ended September 30, 2006 to approximately $997 for the nine months ended September 30, 2007. This increase is attributable to the additional financing required for the capital expenditures of $789 for new store openings and the extra inventory of $221 needed for these stores and to the imputed interest on the increased long-term debt from the shareholder. The long-term debt from the same holder increased from $2,676 as of September 30, 2006 to $ 3,785 as of September 30, 2007 while the related imputed interest increased from $236 in 2006 to $485 in 2007.

Income tax provision increased from approximately $259 for the nine months ended September 30, 2006 to approximately $812 for the nine months ended September 30, 2007 due to our higher profits. The effective tax rate was 32% for both 2006 and 2007.

Net income increased from approximately $117 for the nine months ended September 30, 2006 to a profit of approximately $959 for the nine months ended September 30, 2007. This increase was primarily attributable to the changes described above.

Table of Contents

CI Companies

Combined Statements of Income

For the Twelve Months Ending December 31, 2006 and 2005

(In thousands CDN $)

	Twelve Months Ended December 31, 2006		Twelve Months Ended December 31, 2005	
Net sales	$ 34,658	100.0%	$ 29,283	100.0%
Cost of sales	12,852	37.1%	11,466	39.2%
Gross profit	21,806	62.9%	17,817	60.8%
OPERATING EXPENSES				
Selling	11,849	34.3%	9,819	33.5%
Warehouse and Distribution	3,446	9.9%	2,439	8.3%
General and Administrative	5,178	14.9%	4,786	16.4%
Operating income	1,333	3.8%	773	2.6%
Interest expense	1,151	3.3%	642	2.2%
INCOME BEFORE INCOME TAXES	182	0.5%	131	0.4%
Income tax provision	271	0.8%	138	0.4%
NET (LOSS)	$ (89)	(0.3)%	$ (7)	0.0%

Twelve months ended December 31, 2006 compared with twelve months ended December 31, 2005.

Net sales for the twelve months ended December 31, 2006 were approximately $34,658, a $5,375 or 18.4% increase from the sales of approximately $29,283 for the twelve months ended December 31, 2005.

Retail sales for the year increased to $22,014 from $15,596. This increase of $6,418 is attributable to the increase in comparable store sales of $1,568, or 10% with the balance of the increase due to the opening of six additional stores during the year for a total of 26 stores open as at December 31, 2006. The increase in comparable sales can be attributed to concentrated efforts to consistently and reliably provide high quality service and product. During the period, American Apparel expanded its fabric offerings which facilitated introduction of new styles across the wholesale and retail distribution channels. As many as thirty new styles were added to the retail distribution channel of which the most notable was the addition of denim products. Staff attendance to customer needs and our increasing product assortment has generated loyalty from repeat customers and has sparked interest in consumers new to American Apparel through word of mouth.

Wholesale sales decreased to $12,644 in 2006 from $13,687 in 2005 for a total decrease of $1,043 or 7.6%. This decrease can be attributed to the change of focus to our retail activities from our wholesale operations.

Gross profit increased 22.4% from approximately $17,817 for the twelve months ended December 31, 2005 to approximately $21,806 for the twelve months ended December 31, 2006. Retail gross profit has increased to $16,963, or 77% of sales, for 2006 from $11,840, or 76% of sales, for 2005. Wholesale gross profit decreased to $4,843, or 38% of sales, in 2006 from $5,977, or 44% of sales, in 2005. The decrease in our wholesale gross profit percentage can be attributed mainly to lower pricing due to the highly competitive nature of the industry in Canada. The increase in the over all gross profit to 63% of sales in 2006 from 61% of sales in 2005 can be attributed to a greater percentage of total sales coming from retail with a higher gross profit percentage. In 2006 retail sales accounted for 64% of total sales and in 2005 retail sales accounted for just 53% of total sales.

General and administrative expenses increased from $4,786 for the year ended December 31, 2005 to $5,178 in the year ended December 31, 2006. This increase was mainly due to the fact that retail general and

administrative increased from $1,245 in 2005 to $2,209 in 2006. Retail management fees increased to $1,620 in 2006 from $700 in 2005. Wholesale general and administrative expenses decreased to $2,969 in 2006 from $3,540 in 2005. Wholesale general and administrative salaries and wages increased from $811 in 2005 to $1,187 in 2006. Administrative salaries went up because of the additional personnel required due to the growth of the company. Offsetting this increase was a decrease in wholesale management fees which decreased from $1,598 in 2005 to $700 in 2006 and this accounted for the majority of the decrease in overall wholesale general and administrative expenses.

Selling expenses increased to $11,848 in 2007 from $9,819 in 2006. Retail selling expenses increased to $11,167 in 2006 from $8,873 in 2005. Retail selling rent increased to $3,833 in 2006 from $2,650 in 2005 due to the additional stores opened in 2006. Retail advertising and promotion increased to $938 in 2006 from $543 due to our efforts to both build awareness and promote new and existing stores. Retail selling depreciation and amortization increased to $1,373 in 2006 from $886 in 2005 due to the additional capital expenditures for the new stores that we opened during the year. Retail salaries and wages increased by $139 mainly due to the opening of six new stores and the increase in sales volume in our existing stores. Wholesale selling expenses decreased to $681 in 2006 from $946 in 2005 mostly due to the reduction of our wholesale advertising and promotion by $260. This reduction was due to a redirection of some of our advertising from wholesale to retail.

Warehouse and distribution expenses increased to $3,446 in 2006 from $2,439 in 2005. Retail warehouse and distribution expenses increased to $1,324 in 2006 from $513 in 2005. This increase was due to an increase in retail warehouse salaries of $1,066. The increase in retail warehouse salaries is attributable to the expansive growth of the company and the additional stores opened during the year. Wholesale warehouse and distribution expenses increased to $2,122 in 2006 from $1,927 in 2005, Wholesale warehouse salaries increased by $177 from $1,277 in 2005 to $1,454 in 2006. This increase was due to wholesale warehouse staff that support both retail and wholesale operations.

Interest expenses increased from approximately $642 for the twelve months ended December 31, 2005 to approximately $1,151 for the twelve months ended December 31, 2006. This increase is attributable to the additional financing required for the capital expenditures of $1,642 incurred in opening new stores during the year the additional inventory of $600 required to stock the new stores and the increase in imputed interest on shareholders long-term debt. The long-term debt from the shareholder increased from $1,825 in 2005 to $5,098 in 2006 while the related imputed interest increased from $185 in 2005 to $323 in 2006.

Income tax provision increased from approximately $138 for the twelve months ended December 31, 2005 to approximately $271 for the twelve months ended December 31, 2006 due to the higher pre-tax income and the higher non-deductible imputed interest as discussed above. The effective tax rate for both years was 32%.

Net loss increased from approximately $7 for the twelve months ended December 31, 2005 to a loss of approximately $89 for the twelve months ended December 31, 2006. This increase was primarily attributable to the increase in salaries, rent and interest as described above.

Table of Contents

CI Companies

Combined Statements of Income

For the Twelve Months Ending December 31, 2005 and 2004

(In CDN $)

	Twelve Months Ended December 31, 2005		Twelve Months Ended December 31, 2004 (Unaudited)	
Net sales	$ 29,283	100.0%	$ 17,379	100.0%
Cost of sales	11,466	39.2%	8,786	50.6%
Gross profit	17,817	60.8%	8,593	49.4%
OPERATING EXPENSES				
Selling	9,819	33.5%	3,261	18.7%
Warehouse and Distribution	2,439	8.3%	1,276	7.4%
General and Administrative	4,786	16.4%	3,531	20.3%
Operating income	773	2.6%	525	3.0%
Interest expense	642	2.2%	343	2.0%
INCOME BEFORE INCOME TAXES	131	0.4%	182	1.0%
Income tax provision	138	0.4%	71	0.4%
NET (LOSS) INCOME	$ (7)	0.0%	$ 111	0.6%

Twelve months ended December 31, 2005 compared with twelve months ended December 31, 2004 (unaudited)

Net sales for the twelve months ended December 31, 2005 were approximately $29,283, an $11,904 or 68.5% increase from the sales of approximately $17,379 for the twelve months ended December 31, 2004.

Retail sales for the year increased to $15,596 from $4,004. This increase of $11,592 is attributable to the increase in comparable store sales of $1,051, or 26% with the balance of $10,541 the increase due to the opening of 11 additional stores during the year for a total of 20 stores at December 31, 2005. The main contributing factor in the increase of retail sales from 2005 to 2006 is due to the greater variety of items being sold at our stores. We went from approximately 6,000 SKU s as at December 31, 2004 to approximately 12,000 SKU s as at December 31, 2005.

Wholesale sales increased to $13,687 in 2005 from $13,374 in 2004 for a total increase of $313 or 2.3%.

Gross profit increased 107.3% from approximately $8,593 for the twelve months ended December 31, 2004 to approximately $17,817 for the twelve months ended December 31, 2005. Retail gross profit has increased to $11,840, or 76% of sales, for 2005 from $2,585, or 65% of sales, for 2004. Wholesale gross profit decreased to $5,977, or 44% of sales, in 2005 from $6,007, or 45% of sales, in 2004. The increase in retail gross profit percentage is due to our higher pricing that we implemented after gaining experience from our first full year in retail in 2004. The decrease in our wholesale gross profit percentage can be attributed mainly to lower pricing due to the highly competitive nature of the industry in Canada. The increase in the over all gross profit to 61% of sales in 2005 from 49% of sales in 2004 can be attributed to a greater percentage of total sales coming from retail with a higher gross profit percentage. In 2005 retail sales accounted for 53% of total sales and in 2004 retail sales accounted for just 23% of total sales.

General and administrative expenses increased to $4,786 for the year ended December 31, 2005 from $3,531 for the year ended December 31, 2004. Administrative salaries increased from $1,814 in 2004 to $2,298 in 2005. Professional fees increased to $499 in 2005 from $305 in 2004. Management fees paid to the shareholder increased to $2,298 in 2005 from $1,814 in 2004.

Table of Contents

Selling expenses increased from approximately $3,261 for the twelve months ended December 31, 2004 to approximately $9,819 for the twelve months ended December 31, 2005. Salaries and wages increased by $2,565 mainly due to the opening of eleven new stores and the increase in sales volume in our existing stores. Rent increased by $2,151 due to the opening of new stores. Advertising and promotion increased by $686 due to our successful efforts to both build awareness and promote new and existing stores Depreciation and amortization expenses increased from approximately $225 for the twelve months ended December 31, 2004 to approximately $914 for the twelve months ended December 31, 2005. This increase was due to the additional capital expenditures necessitated by the opening of 11 new stores in 2005.

Warehouse and distribution expenses increased to $2,439 in 2005 from $1,276 in 2004. Warehouse salaries increased by $682 in 2005 due to the increased labor force required to service the more than doubling of our retail outlets during the year.

Interest expense increased from approximately $343 for the twelve months ended December 31, 2004 to approximately $642 for the twelve months ended December 31, 2005. This increase is attributable to the additional financing required for the capital expenditures of $3,441 incurred in opening of new stores the additional inventory of $1,751 required to stock the new stores and the increase in the imputed interest on the shareholder s long-term debt. The long-term debt from the shareholder increased from $812 in 2004 to $1,825 in 2005 while the related imputed interest increased from $73 in 2004 to $185 in 2005.

Income tax provision increased from approximately $71 for the twelve months ended December 31, 2004 to approximately $138 for the twelve months ended December 31, 2005 due to the higher non-deductible imputed interest as discussed above. The effective tax rate on taxable income for both years was 32%.

Net profit decreased from approximately $111 for the twelve months ended December 31, 2004 to a loss of approximately $7 for the twelve months ended December 31, 2005. This decrease was primarily attributable to the increase in expenses necessitated by our rapid retail expansion.

Liquidity and Capital Resources

Liquidity and Capital Resources AAI

American Apparel generally funds its operations and working capital needs through cash generated from operations and borrowings under its credit facilities, term loans and promissory notes.

The typical cash flow cycle from operations is as follows:

Yarn inventory is purchased to meet expected demand plus a safety stock. The yarn supplied from the United States and Mexico is generally purchased directly from the yarn mills while yarn from Pakistan and other countries is purchased through yarn brokers. Payment terms for these vendors average 60 days from the date the product ships from the mill in the United States or Mexico and from other sources, from the US warehouse or US entry point of direct shipments. Increased sales have resulted in increased levels of inventory, and therefore an increase in the amount of cash required to fund inventory levels. The growth in the number of worldwide retail stores has resulted in increased levels of finished goods inventory at retail and back up inventory at the distribution centers. The need to respond quickly to trends and product demand has also resulted in higher inventory levels at the intermediate stages, greige goods and dyed fabrics, to permit faster product completion in our vertically integrated manufacturing system. The seasonality of our products in both the retail and wholesale channels would generally result in an overall inventory buildup in the first quarter to be positioned properly to support sales in the second and third quarters.

Sales to wholesale customers generally have payment terms of 30 days. The increased sales have resulted in an increase in the level of accounts receivable, and therefore have increased the amount of cash required to fund working capital.

Table of Contents

A summary of inventory and trade accounts receivable for AAI were as follows:

	September 30, 2007 (Unaudited)	December 31, 2006	December 31, 2005	December 31, 2004 (Unaudited)
Inventory	$ 91,324	$ 76,470	$ 67,534	$ 47,072
Trade Receivables	20,497	13,969	12,111	12,035

As of September 30, 2007, and December 31, 2006, 2005 and 2004, AAI maintained an allowance for doubtful accounts of $1,997, $2,163, $1,085 and $864, respectively. For the same periods, AAI s provision for slow moving inventories was $4,284, $4,284, $800 and $200, respectively. AAI s allowance for doubtful accounts as a percentage of trade receivables decreased from approximately 15% at December 31, 2006 down to approximately 10% at September 30, 2007. This decrease is due to several key factors. A certain portion of the aged trade accounts receivable associated with AAI s foreign operations were written off against the allowance for doubtful accounts after they were deemed uncollectible. In addition, parallel with its expansion into international markets, AAI has experienced an improvement in accounts receivable turnover during the six month period ended September 30, 2007 which allowed for an adjustment in the estimate for the allowance for doubtful accounts.

A summary of inventory and accounts receivable for the CI companies (in CDN$):

	September 30, 2007 (unaudited)	December 31, 2006	December 31, 2005	December 31, 2004 (unaudited)
Inventory	$ 7,069	$ 8,162	$ 7,393	$ 5,447
Trade Receivables	1,763	1,317	2,536	1,500

As of September 30, 2007, and December 31, 2006, 2005 and 2004, the CI companies maintained an allowance for doubtful accounts of CDN$61, CDN$30, CDN$32 and CDN$48, respectively.

American Apparel has been able to fund its increased working capital through an asset-based line of credit with a bank. The lender follows a borrowing base formula that allows advances based on the levels of accounts receivable and inventory and various other conditions. In addition, American Apparel also has term loans with banks and various notes payable.

A major portion of capital expenditures for American Apparel are for production machinery and information systems. Decisions to purchase equipment and machinery are based upon the planning for required inventory levels. Certain types of equipment are more efficient at production of certain styles so that the desired inventory mix may also influence the decisions made regarding the types of equipment and machinery that are being purchased.

Another major portion of capital expenditures are made for leasehold improvement costs related to retail store openings as well as for continuing store operations. These leasehold improvements are capitalized of the shorter of either the life of the lease or the useful lives of improvements.

Going forward, American Apparel s management believes that it will be successful in obtaining additional funding and if necessary, negotiating waivers to certain loan covenants with its existing lenders. However, no assurance can be provided that American Apparel will obtain the additional funding or that its lenders will grant waivers if there are further covenant violations.

American Apparel s strategy for funding its business going forward is a combination of the following: increased profitability; increased borrowing lines as required with traditional lenders (asset-based); and utilization of the proceeds available from the business combination with Endeavor to fund its business as well as

potential acquisitions. These proceeds could potentially be used to pay off the existing debt; fund working capital increases; fund acquisitions of other businesses and pay dividends to current AAI stockholders for their income tax liabilities. Even if the existing debt is paid down, it is likely that AAI will continue to maintain available lines of credit on an asset-backed basis in order to fund working capital needs in the future.

Over the past year, AAI s growth has been funded through a combination of borrowings from related and unrelated parties, bank debt and lease financing. As of September 30, 2007 AAI had approximately $6.5 million in unrestricted cash. On January 18, 2007, AAI completed a $41 million secured debt financing with SOF Investments. During July 2007, AAI executed an agreement to obtain an additional $10 million in financing from SOF Investments. During July 2007, AAI also replaced its revolving credit facility of $62.5 million with an increased revolving facility of $75 million from LaSalle Bank. AAI believes that as a result of this it currently has sufficient cash and financing commitments to meet its funding requirements through at least September 2008. AAI expects that it will need to obtain additional financing in order to accomplish its business plan over the next several years. There can be no assurance as to the availability or terms upon which such financing might be available.

Cash Flow Overview AAI

For the nine months ended September 30, 2007, cash used in operations was $12,629. This is a result of income from operations before non-cash expenses (depreciation and amortization, deferred rent expense and bad debt expense) of $8,750 offset by the increase in inventory of $14,499, increase in receivables of $3,183, increase in prepaid expenses and other assets of $3,926, decrease in accounts payable and accrued expenses of $13,670 and an increase in income taxes payable of $2,840. Cash used in operations was primarily used to reduce obligations to trade and other vendors. Cash used in operations was also used to finance an increase in inventory production levels during the first two quarters of 2007 through raw material purchases to support AAI s peak selling season that generally occurs from the months of May through September. This was evident through increase in cash used for production selling and administrative staff payroll.

For the nine months ended September 30, 2007, AAI used $10,892 of cash in investing activities. This is a result of increased investment in property and equipment for the wholesale segment by approximately $1,196 and an increased investment in property and equipment of $9,696 for the retail and other segments. During the period, AAI invested in new cutting, sewing, information systems equipment required to support the increased production levels experienced during the period. Increase in investment in property and equipment for the retail segment was due to the 15 new retail stores that were opened in the nine months ended September 30, 2007.

For the nine months ended September 30, 2007, cash from financing activities was $26,600. This is a result of increases to the line of credit of $1,542, increases to the term loans and notes payable of $53,981 offset by payments to term loans and notes payable of $21,711, payments for capital lease obligations of $2,518 and distributions and advances to stockholders of $4,736. AAI s principal capital requirements are to fund working capital needs and to finance opening of new retail stores, as well as to finance purchase of new manufacturing and information systems equipment to support higher production levels and growth in online operations.

For the year ended December 31, 2006, cash provided by operations was $9,886. This is a result of income from operations before non-cash expenses (depreciation and amortization, inventory reserve and deferred rent expense) of $13,454 offset by the increase in inventory of $12,010, increase in deposits and other assets of $4,596 and the increase in accounts payable and accrued expenses of $13,253. Cash proved by operations was a direct result of buildup in trade payables due to liquidity issues in late 2006 until additional, long-term financing was secured. This financing was completed in January 2007.

For the year ended December 31, 2006, cash used in investing activities was $15,232. This is a result of investments in property and equipment for the wholesale segment by $4,288 and $10,944 for the retail and other

Table of Contents

segments to support the growth of AAI. The retail segment opened 41 new stores during the year ended December 31, 2006. During the period, AAI invested in leasehold improvements to support buildouts and opening of new retail stores.

For the year ended December 31, 2006, cash from financing activities was $6,001. This is a result of increases to the line of credit of $6,643, increases in term loans and notes payable of $11,885 offset by payments to term loans and notes payable of $7,803, payments to capital lease obligations of $3,141 and distributions and advances to stockholders of $1,091. AAI s principal capital requirements are to fund working capital needs and to finance opening of new retail stores, as well as to finance purchases of new manufacturing and information systems equipment in order to support higher production levels and growth in online operations.

For the year ended December 31, 2005, cash used in operations was $1,116. This is a result of income from operations before non-cash expenses (depreciation and amortization, inventory reserve and deferred rent expense) of $14,612 offset by the increase in inventory of $20,824, increase in receivables of $1,588, increase in prepaid expenses, deposits and other assets of $3,444 and the increase in accounts payable and accrued expenses of $9,819. Cash used in operations was used to reduce obligations to vendors and to finance an increase in inventory levels through increased raw material purchases and payroll expenses in order to support AAI s peak selling season that generally occurs from the months of May through September.

For the year ended December 31, 2005, cash used in investing activities was $15,859. This is a result of additional investing in property and equipment for the wholesale segment by $2,695 and $11,940 for the retail and other segments. The retail segment opened 56 new stores during the year ended December 31, 2005. During the same year, AAI also purchased the net assets including all of its dyeing equipment and lease agreement of the E & J Textile Group fro $1,224. These assets were used to organize a subsidiary and start a dyeing facility (American Apparel Dyeing and Finishing, Inc.).

For the year ended December 31, 2005, cash from financing activities was $17,428. This is a result of increases to the line of credit of $10,220, increases to term loans and notes payable of $12,046 offset by payments to term loans and notes payable of $2,229, payments to capital lease obligations of $3,659, distributions and advances to stockholders of $1,951 and increases to cash overdraft by $2,385. AAI s principal capital requirements are to fund working capital needs and to finance opening of new retail stores, as well as to finance purchases of manufacturing equipment and information systems to support increased production levels.

For the year ended December 31, 2004, cash used in operations was $16,607. This is a result of income from operations before non-cash expenses (depreciation and amortization, provisions for bad debts, inventory reserve and deferred rent expense) of $11,348 offset by the increase in inventory of $26,438, increase in receivables of $5,907, increase in prepaid expenses and other assets of $1,537 and the increase in accounts payable and accrued expenses of $5,518. Cash used in operations was used to reduce obligations to vendors and to finance an increase in inventory levels to support AAI s peak selling season that generally occurs from the months of May through September.

For the year ended December 31, 2004, cash used in investing activities was $9,896. This is a result of increasing property and equipment for the wholesale segment by $4,970 and $4,926 for the retail segment. The retail segment opened 25 new stores during the year ended December 31, 2004. Investments in retail stores primarily included buildouts of leasehold improvements and store equipment.

For the year ended December 31, 2004, cash from financing activities was $27,756. This is a result of increases to the line of credit of $31,705, increases to term loans and notes payable of $11,093 offset by payments to term loans and notes payable of $415, payments to capital lease obligations of $412, distributions and advances to stockholders of $1,510, increases to cash overdraft of $1,301 and decreases to matured funds from factor of $14,711. AAI s principal capital requirements are to fund working capital needs and to finance opening of new retail stores, as well as purchases of manufacturing equipment and information systems to support increased production levels.

Table of Contents

Cash Flow Overview The CI Companies (in CDN$)

For the nine months ended September 30, 2007 CI companies had cash provided by operating activities as compared to cash used in operating activities for the nine months ended September 30, 2006. This improvement was due in large part to the increased profitability of CI companies and the improved management of operating assets. As well, they did not open any new stores in the first half of 2007 so their cash requirements for additions to capital expenditures were reduced and their funds were used mainly to repay bank indebtedness. On September 30, 2007 their bank indebtedness was $885 with a credit facility allowing maximum borrowings of $4,500.

On September 30, 2007 their working capital was $2,263 as compared to negative working capital of $182 in 2006. Accounts receivable days outstanding improved to 47 days as at September 30, 2007 from 57 in 2006. Inventory decreased to $7,069 in 2007 from $8,948 in 2006. Inventory turnover has increased to 1.9 times in 2007 from 1.5 times in 2006.

Cash provided by operating activities for the nine months ended September 30, 2007 was $5,961 as compared to cash used in operating activities of $117 for the nine months ended September 30, 2006. Cash used in investing activities was $2,118 representing property and equipment additions for this year together with advances given to the U.S. affiliate. In 2006 the cash used in investing activities was $937 and this was only related to additions to property and equipment.

Cash used in financing activities was $4,146 in 2007 versus cash provided of $1,032 in 2006. In 2007 this represented a pay down of bank indebtedness by CI companies as compared to an increase in bank indebtedness and long-term debt in 2006 which provided the bulk of their financing. This resulted in a decrease in cash of $303 for the nine months ended September 30, 2007.

CI companies   principal capital requirements are to fund working capital needs and to open new stores. These capital requirements have generally been satisfied by a combination of borrowings under their credit facility and the issuance of long-term debt to related parties. On December 31, 2006, their bank indebtedness was $3,821 with a credit facility having maximum borrowings of $4,500.

In 2006 working capital was $1,795 as compared to negative working capital of $248 in 2005. Accounts receivable days outstanding improved to 38 days in 2006 from 68 in 2005. Inventory increased to $8,162 in 2006 from $7,393 in 2005 mainly due to the opening of 6 new stores during 2006. Inventory turnover has decreased to 1.7 times in 2006 from 1.8 times in 2005.

Cash used in operating activities for the year ended December 31, 2006 was $518 as compared to cash provided by operating activities of $128 for the year ended December 31, 2005. Cash used in investing activities was $1,881 representing property and equipment additions for this year, which were primarily related to the build out of six new stores. In 2005 the cash used in investing activities was $3,908 and was primarily related to the build out of 11 new stores.

Cash provided by financing activities was $2,814 in 2006 versus $4,025 in 2005. In both years the bulk of the financing has been provided by a combination of bank indebtedness and issuance of long-term debt. This resulted in an increase in cash of $414 for the year.

In 2005, CI companies principally financed its operations through a combination of borrowings under their credit facility and through the issuance of long-term debt. The long-term debt was issued both by related parties and from their bankers. The principal use of these funds was for the additions to capital assets necessitated by their opening of 11 new stores during the year. In 2004 our principal use of funds was also for capital expenditures for the opening of 8 new stores.

Table of Contents

In 2005 working capital was negative $248 as compared to negative working capital of $444 in 2004. Accounts receivable days outstanding increased to 68 days in 2005 from 41 days in 2004. Inventory increased to $7,393 in 2005 from $5,447 in 2004 mainly due to the opening of 11 new stores during 2005. Inventory turnover has decreased to 1.8 times in 2005 from 2.0 times in 2004.

Cash provided by operating activities for the year ended December 31, 2005 was $128 as compared to $1,615 for the year ended December 31, 2005. Cash used in investing activities was $3,908 representing property and equipment additions for this year, which were primarily related to the build out of 11 new stores, as compared to $3,339 in 2004 which was used primarily for the build out of 8 new stores.

Cash provided by financing activities was $4,025 in 2005 versus $1,724 in 2004. In both years the bulk of the financing has been provided by a combination of bank indebtedness and issuance of long-term debt. This resulted in an increase in cash of $246 for the year.

Obligations Overview AAI

Over the past year, AAI s growth has been funded through a combination of borrowings from related and unrelated parties, bank debt and lease financing. As of September 30, 2007 AAI had approximately $6,490 in unrestricted cash. On January 18, 2007, AAI completed a $41 million secured debt financing with SOF Investments. During July 2007, AAI executed an agreement to obtain an additional $10 million in financing from SOF Investments. During July 2007, AAI also replaced its revolving credit facility of $62,500 with an increased revolving facility of $75,000 from LaSalle Bank. AAI believes that as a result of this it currently has sufficient cash and financing commitments to meet its funding requirements through at least September 2008 based upon matching store openings to available funding. AAI expects that it will need to obtain additional financing in order to accomplish its business plan over the next several years. There can be no assurance as to the availability or terms upon which such financing might be available.

Debt Agreements

The following is an overview of AAI s long term and current debt as of September 30, 2007.

Description of Debt	Lender Name	Interest Rate	September 30, 2007	Covenant Violations	Reference
Revolving Credit Line	LaSalle Bank	LIBOR + 2.0%	$ 50,110	Yes	a
Term loan from private investment firm	SOF Investments	16.0%	51,000	Yes	b
Term Loan	South Bay Bank	Prime + 1.00%	249		c
Long-Term Equipment Loans	3 loans for equipment and vehicles ranging between $5 - $26	From 4.6% to 11.9%	46		d
Leasehold Improvement Loans	2 loan from landlords ranging between $90 -$655	From 8% to 9%	746		e
Long-Term Software Loan	De Lage Landen Financial	9.0%	320		f
Total Long Term Bank Debt			102,471		
Less current portion of bank debt			365		
Long-Term bank debt, net of current portion			102,106		
Notes payable to related parties	Six individual notes to shareholder and family members	From 12% to 18%	4,380		g
Notes payable to unrelated parties	Thirty four individual notes to individuals ranging between $10 -$500	From 12% to 24%	5,639		h
Subordinated notes payable to related parties	Two notes to shareholder and family member	From 12% to 18%	360		i
Capital lease obligations	72 individual leases ranging between $1 - $428	From 8% to 24%	6,772		j
Total debt			119,257		
Cash Overdraft			4,858		

Total Net debt	$	124,115

189

Table of Contents

a) At September 30, 2007, revolving credit facility with LaSalle Bank provided for borrowings up to $75,000. Borrowings under the facility are subject to certain advance provisions established by the bank and are collateralized by substantially all assets of AAI. Interest under the agreement is at LIBOR (5.72% at September 30, 2007) plus 2.0% or the bank s prime rate (8.25% at September 30, 2007), at AAI s option. The interest rate was 7.72% at September 30, 2007. The facility was to expire in January 2010. The average borrowings during the nine months were $50,241. AAI s stockholders personally guaranteed the borrowings. On January 18, 2007, AAI negotiated an increase in the size of its credit facility to $62,500. Among other requirements, this facility agreement included a subjective acceleration clause and required AAI to maintain a lock box. During July 2007, AAI replaced this revolving credit facility with an increased revolving credit facility of $75 million from LaSalle Bank which expires at the earlier of July 2, 2012 or thirty days prior to the maturity date of the loan agreement with the private investment firm (January 18, 2009) unless its refinanced on terms acceptable to the bank. Borrowings under the new facility are subject to certain advance provisions established by the bank and are collateralized by substantially all of the assets of American Apparel. No charges for early extinguishment of debt were incurred associated with this transaction. At September 30, 2007, AAI failed to meet certain covenants relating to its financing agreement with LaSalle Bank. Covenant violations of the LaSalle agreement included issuance of guarantees for leases outside of United States, cash advances to subsidiaries incorporated outside of United States and assignment of certain life insurance proceeds from AAI to the CI companies. These covenant violations triggered a cross default covenant violation with SOF Investments. As a result of these covenant violations, AAI was in default of provisions stipulated in its financing agreements with these two creditors. During November 2007, AAI obtained from LaSalle Bank and SOF waivers for the violation of these covenants effective September 30, 2007 and as at November 2007.

b) On January 18, 2007, AAI completed a $41 million secured debt financing with SOF Investments. The proceeds of the financing were used to repay AAI s subordinated notes payable held by C3 Capital Partners, L.P., of $14,200 (including principal, interest and fees), and to repay its term loans with its bank of $5,600. Net proceeds related to the secured debt financing amounted to approximately $18 million. Indebtedness under the agreement bears interest at 16% per annum, payable monthly and matures on January 18, 2009. The agreement requires AAI to meet certain financial covenants. These covenants include fixed charge coverage ratio, annual capital expense limitation, minimum EBITDA, debt to EBITDA ratio, and adjusted debt to EBITDAR ratio. In the event AAI is in default under the agreement the interest rate increases to 21% per annum and the lender has the right to demand payment in full of all outstanding indebtedness. On July 2, 2007, AAI obtained an additional $10 million secured debt financing with SOF Investments under the same terms as the original agreement dated January 18, 2007. The agreement allows prepayments prior to January 18, 2008 at the present value of all scheduled payments of interest (whether in cash and in-kind) through the first anniversary of the Closing Date in respect of the amount so repaid discounted at a rate equal to the Federal Funds Rate. Subsequent to that date, any prepayment must include a prepayment premium equal to 3% of the amount prepaid. As discussed in (a) covenant violations of the LaSalle financing agreement triggered a cross default covenant violation with SOF Investments. As a result of these covenant violations, AAI was in default of provisions stipulated in its financing agreements with these two creditors. During November 2007, AAI obtained from LaSalle Bank and SOF waivers for the violation of these covenants effective September 30, 2007 and as at November 2007.

c) At September 30, 2007, AAI had two term loans with South Bay Bank. The first loan is payable in monthly installments of $5, including interest at prime (8.25% at September 30, 2007) plus 1% through October 2007. The balance at September 30, 2007 was $5. The second loan is payable in monthly installments of $22, including interest at prime plus 1% through December 2008. The balance at September 30, 2007 was $244. Both of these loans are secured by related equipment.

d) At September 30, 2007, AAI had various promissory notes payable in monthly installments aggregating $18, including interest ranging from 4.6% to 11.9% and maturing at various dates through August 2011. The notes are collateralized by equipment.

e) At September 30, 2007, AAI had two leasehold improvement term loans with certain landlords of its retail stores. The first loan is payable in monthly installments of $3 through March 2010, including interest at a

190

rate of 8%. The balance at September 30, 2007 was $90. The second loan was payable in monthly interest only payments at 9% through December 2009. The balance at September 30, 2007 was $656.

f) At September 30, 2007, AAI has a term loan with De Lage Landen Financial financing company payable in monthly installments of $11 through April 2011, including interest at a rate of 9%. The balance at September 30, 2007 was $320.

g) AAI has unsecured notes payable to certain individuals related to a stockholder, which are due upon demand with interest ranging from 12% to 18% per annum. The balance outstanding at September 30, 2007 was $4,380.

h) AAI has unsecured notes payable to certain unrelated individuals, which are due upon demand with interest ranging from 10% to 24% per annum. The balance outstanding at September 30, 2007 was $5,639. Notes are personally guaranteed by a stockholder of AAI.

i) AAI has unsecured notes payable with a related party (relative of a stockholder), which are due upon demand with interest at 18%. The balance outstanding at September 30, 2007 was $180. The note is subordinated to the interest of the bank which held AAI s current revolving credit facility as well as the interest of the bank which provided the new secured revolving credit facility on July 2, 2007. AAI has an unsecured note payable to a stockholder which is due on demand with interest at 12%. The balance outstanding at September 30, 2007 was $180. The note is subordinated to the interest of the bank which held AAI s current revolving credit facility as well as the interest of the bank which provided the new secured revolving credit facility on July 2, 2007.

j) AAI leases certain equipment under capital lease arrangements expiring at various times through 2011. The assets and liabilities under capital leases are recorded at the lower of the present values of the minimum lease payments or the fair values of the assets.

Contractual Obligations Summary

The following table summarizes AAI s contractual commitments as of September 30, 2007, which relate to future minimum payments due under non-cancelable licenses, leases, long-term debt and advertising commitments. Future minimum rental payment on operating lease obligations presented below do not include any related property insurance, taxes, maintenance or other related costs required by operating leases. Operating lease rent expenses, including the related real estate taxes and maintenance costs, are included in the Cost of sales and General and administrative expenses in AAI s financial statements and amounted to approximately $22,738 for the nine months ending September 30, 2007.

	Payments due by period				
Contractual Obligations	**Total**	**Less than 1 year**	**1-3 years**	**4-5 years**	**More than 5 years**
Long term debt, including interest	$ 125,593	$	$ 125,593	$ 8	$
Current debt, including interest	16,280	16,280			
Capital lease obligations, including interest	7,578	3,573	4,005		
Operating lease obligations	160,846	26,222	$ 43,281	$ 36,091	$ 55,252
Advertising Commitments	1,929	1,929			
Total	$ 312,234	$ 48,004	$ 172,879	$ 36,099	$ 55,252

Over the past year, AAI s growth has been funded through a combination of borrowings from related and unrelated parties, bank debt and lease financing. As of September 30, 2007, AAI had approximately $6,490 in unrestricted cash. As of September 30, 2007, AAI failed to meet certain debt covenants relating to its financing agreements with LaSalle Bank and SOF Investments. Covenant violations of the LaSalle agreement included issuance of guarantees for leases outside of United States, cash advances to subsidiaries incorporated outside of United States and assignment of certain life insurance proceeds from AAI to the CI companies. These covenant violations triggered a cross default covenant violation with SOF Investments. As a result of these covenant

Table of Contents

violations, AAI was in default of provisions stipulated in its financing agreements with these two creditors. During November 2007, AAI obtained from LaSalle Bank and SOF waivers for the violation of these covenants effective September 30, 2007 and as at November 2007.

Obligations Overview The CI Companies (in CDN$)

Long Term and Current Debt

The following is an overview of the CI companies long term and current debt. Payments due on these obligations are summarized in the table of contractual obligations below.

The CI companies have a line of credit facility with maximum borrowings of $4,500, due on demand, bearing interest at the bank s prime rate plus 1% per annum payable monthly. This line of credit is secured by a $5,000 moveable hypothec and provides for a charge on the CI companies accounts receivable, inventory and all other moveable assets and by Section 427 under the Bank Act of Canada on inventory. A movable hypothec is a legal term used in Quebec civil law which is equivalent to the common law term, chattel mortgage. It is a real right on a movable property made liable for the performance of an obligation. It confers on the creditor the right to follow the property into whosoever hands it may be, to take possession of it or to take it in payment, or to sell it or cause it to be sold and, to have a preference upon the proceeds of the sale ranking.

The bank s agreement contains various covenants which require the CI companies to maintain certain financial ratios and commitments as defined by the bank. As at September 30, 2007 and December 31, 2006, the CI companies were not in compliance with certain of these covenants. The bank has waived compliance with the obligation to meet these covenants as at September 30, 2007 and December 31, 2006.

Certain of the CI companies have provided unlimited corporate guarantees to secure this credit facility. These guarantees are secured by either moveable hypothecs in the amount of $3,200 or general assignment agreements.

In addition to the line of credit facility, the CI companies have the following long term debt:

Various bank term loans, repayable in monthly capital installments aggregating $37 plus interest at rates ranging from the bank s prime rate plus 2% to the bank s prime rate plus 3% per annum, maturing at dates ranging from 2008 to 2011. As a result of the reorganization of the retail companies these loans were fully repaid by September 30, 2007. Aggregate balance of these loans was $1,323 at December 31, 2006.

Loan of $450 U.S. from a member of the immediate family of the stockholder, being a director of a company, bearing interest at 18% and without terms of repayment. The loan has been subordinated in favor of the bank. This loan will not be repaid prior to January 1, 2008. Balance of this loan was $524 at December 31, 2006.

Loan of $3,804 U.S. from the stockholder, non-interest bearing and without terms of repayment. An amount of $2,394 U.S. has been subordinated in favor of the bank. The stockholder has agreed to subordinate an additional $1,410 U.S. This loan will not be repaid prior to January 1, 2008. Balance of this loan was $5,098 at December 31, 2006.

Mortgage of $401 maturing November 2009, bearing interest at 4.85% per annum. The mortgage is secured by the building and is repayable in monthly installments of $2, combining principal and interest. Balance of this loan was $408 at December 31, 2006.

Loan of $300 from a member of the immediate family of the stockholder, and a director of a company, bearing interest at 15% and without terms of repayment. The loan has been subordinated in favor of the bank. This loan will not be repaid prior to January 1, 2008. Balance of this loan was $300 at December 31, 2006.

Loan of $42 from an individual, bearing interest at 14%, repayable in blended monthly payments of $21, maturing in 2007. Balance of this loan was $219 at December 31, 2006.

192

Table of Contents

Debt Agreements

The following is an overview of CI companies long term and current debt as of September 30, 2007

Description of Debt	Lender Name	Interest Rate	September 30, 2007	Covenant Violations	Reference
Revolving demand credit facility $4,500	Toronto Dominion Bank	Canadian prime plus 1%	$ 885	Yes	a
Mortgage	HSBC	4.85%	401		
Various loans	Various*	14 - 18%	4,574		
			$ 5,860		

* Lenders referred to as various include a 4 of debt agreements with individual debt amounts in the range from $92 to $3,785.

a) The revolving demand credit facility is secured by the accounts receivable, inventory and all moveable assets of the companies. The shareholder has subrogated US$2,394 and a relative of the shareholder has subrogated $1,410 in favor of the bank. The shareholder has provided an unlimited personal guarantee in favor of the bank. A relative of the shareholder has provided a personal guarantee in the amount of US$450 in favor of the bank.

As at September 30, 2007 the company was not in compliance with the Minimum Net Working Capital covenant required by the bank. The bank has waived compliance with the obligation to meet this covenant. The company is presently negotiating with its bank to revise these covenants as part of its annual renewal of the banking agreement.

Contractual Obligations Summary

The following table summarizes the CI companies contractual commitments as of September 30, 2007, which relate to future minimum payments due under non-cancelable licenses, leases and other debt (in CDN$). Future minimum rental payment on operating lease obligations presented below do not include any related property insurance, taxes, maintenance or other related costs required by operating leases. Operating lease rent expenses, including the related real estate taxes and maintenance costs, are included in the Cost of sales and General and administrative expenses in CI companies financial statements and amounted to approximately $3,553 for the nine months ending September 30, 2007.

	Payments due by period					
Contractual Obligations	Total	Less than 1 year	1-3 years	4-5 years	More than 5 years	No fixed terms of repayment
Long term debt, excluding interest	$ 4,975	$ 52	$ 391	$	$	$ 4,532
Interest	42	20	22			
Capital lease obligations, excluding interest	13	13				
Interest	1	1				
Operating lease obligations	22,103	3,492	6,287	5,222	7,102	
Total	$ 27,134	$ 3,578	$ 6,700	$ 5,222	$ 7,102	$ 4,532

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors, except for the financing commitments previously discussed.

193

Table of Contents

American Apparel Related Party Transactions

The following is a summary of transactions since January 1, 2006 to which American Apparel has been a party in which the amount involved exceeded $120,000 and in which any of American Apparel s executive officers, directors or stockholders had or will have a direct or indirect material interest.

Lim Buyout Agreement

Each of AAI and Messrs. Charney and Lim are parties to an agreement, dated as of November 9, 2006, pursuant to which Mr. Charney shall purchase all of the outstanding capital stock and membership interests of the American Apparel companies held by Mr. Lim in the Lim Buyout for $60 million in cash, plus an additional cash price equal to (1) $60 million divided by 365, (2) multiplied by 0.20, (3) multiplied by the number of days after May 1, 2007 the Lim Buyout is consummated. In the event that the Lim Buyout is not consummated by Mr. Charney prior to closing of the acquisition for any reason, Endeavor shall effect the Lim Buyout as part of the acquisition by paying Mr. Lim cash for all of his equity interests in the American Apparel companies. Since there is no economic incentive for Mr. Charney to effect the Lim Buyout, Endeavor will effectively be required to effect the Lim Buyout. If the acquisition were to be consummated on December 14, 2007, and Endeavor was required to effect the Lim Buyout on the same date, Endeavor would pay Mr. Lim approximately $67.8 million.

Employment Agreements

American Apparel has not entered into employment agreements or any other written employment arrangements with any of its named executive officers. American Apparel is a party to an employment agreement with one of its non-executive officers. The employment agreement provides that the executive is an at-will employee and her employment may be terminated at any time by the employee or the company upon notice. The employee s base salary under the employment agreement is $150,000 and the employee shall be entitled to a vested guaranteed bonus of $37,500, payable each May 31st and December 31st. The initial term of the agreement is one year, such term to be automatically renewed for successive one-year period unless earlier terminated in accordance with the agreement. Under the employment agreement, the officer is entitled to participate in American Apparel s general employee benefit plans in accordance with the terms and conditions of such plans. The employment agreement also provides the officer with certain severance benefits.

Table of Contents

Unsecured Indebtedness

American Apparel is currently indebted to its stockholders, certain key employees, and/or relatives of its stockholders in an aggregate principal amount of approximately $12.0 million. All of the unsecured indebtedness is due on demand by the holder of the underlying notes. Upon consummation of the acquisition, these amounts will be immediately paid. The specifics of each of the notes issued to the related parties are as follows as at September 30, 2007:

Name of Noteholder	Principal Amount of Note Outstanding as of the date hereof		Annual Interest Rate
Moshe Safdie & Associates (architecture firm principally owned by Mr. Charney s uncle)	$	2,718	18%, paid monthly
Sylvia Safdie (Mr. Charney s mother)	$	832	12%, compounded monthly
Maya Charney (Mr. Charney s sister)	$	56	12%, compounded monthly
Gabriel Safdie (Mr. Charney s uncle)	$	121	18%, paid monthly
Kelley Devanathan (employee of AAI)	$	23	18%, compounded monthly
Ronite Sasson (employee of CI)	$	284	18%, compounded monthly
Martin Bailey (officer of AAI)	$	116	18%, paid monthly
Adrian Kowalewski (employee of AAI)	$	35	18%, paid monthly
Rod Kazazi (employee of AAI)	$	100	18%, paid monthly
Louis Canadas (employee of AAI)	$	80	18%, paid monthly
Sam Lim	$	180	12%, paid monthly (subordinated)
Morris Charney (Mr. Charney s father)	$	180	18%, paid monthly (subordinated)
	$	2,198	18%, paid monthly
Dov Charney	$	4,027	18%, paid monthly
David Kim (employee of AAI)	$	150	18%, paid monthly
Lloyd Brown (director of CI)	$	42	14% blended monthly payments
Paul Willianson (relative of employee)	$	50	12%, compounded monthly
Four-Two-Three (company owned by relative of employee)	$	250	18%, compounded monthly
Members of Kapadia Family (relatives of employee)	$	121	18%, compounded monthly
Billy Mauer (Mr. Charney s cousin)	$	500	18%, compounded monthly

Property Leases

Mr. Charney and/or AAI have guaranteed the obligations of American Apparel under various property leases, including:

New York store at 712 Broadway, New York, NY for up to approximately $820,000 in aggregate obligations;

New York store at 183 E. Houston St. New York, NY for up to approximately $430,000 in aggregate obligations;

New York store at 1090 Third Ave., New York, NY for up to approximately $190,000 in aggregate obligations;

Chicago store at 1563 N. Milwaukee Ave., Chicago, IL for up to approximately $213,000 in aggregate obligations;

Los Angeles store at 6922 Hollywood Blvd., Los Angeles, CA for up to approximately $2.2 million in aggregate obligations; and

195

Table of Contents

Montreal store at 3521, 3523 and 3525 St. Laurent Blvd., Montreal Quebec HTX2T6 for up to approximately C$514,000 in aggregate obligations.

In December 2005, American Apparel entered into an operating lease, which commenced on November 15, 2006, for its knitting facility with American Central Plaza, LLC. Mr. Charney and Mr. Lim s spouse each hold a 25% membership interest in American Central Plaza. The remaining members of American Central Plaza are not affiliated with American Apparel. The monthly lease payments are $48 and the lease expires in November 2011, with a five year extension, at the option of American Apparel. A number of the property leases entered into by American Apparel require the consent of the lessor in the event of a change of control.

Inflation

Inflation affects the cost of raw materials, goods and services used by AAI. In recent years, inflation has been modest. However, high oil costs can affect the cost of all raw materials and components. The competitive environment somewhat limits the ability of AAI to recover higher costs resulting from inflation by raising prices. Although AAI cannot precisely determine the effects of inflation on its business, it is management s belief that the effects on revenues and operating results have not been significant. AAI seeks to mitigate the adverse effects of inflation primarily through improved productivity and strategic buying initiatives. AAI does not believe that inflation has had a material impact on its results of operations for the periods presented, except with respect to payroll-related costs and other costs arising from or related to government imposed regulations.

Financial Covenants and Credit Rating

AAI s credit arrangements impose certain restrictions on AAI regarding capital expenditures and limit AAI s ability to: incur additional indebtedness, dispose of assets, make repayments of indebtedness or amendments of debt instruments, pay distributions, create liens on assets and enter into sale and leaseback transactions, investments, loans or advances and acquisitions. Such restrictions could limit AAI s ability to respond to market conditions, to provide for unanticipated capital investments or to take advantage of business or acquisition opportunities. AAI is in compliance with all covenants under its credit arrangements at September 30, 2007.

Seasonality

AAI experiences seasonality in its operations. Historically, sales during the second and third fiscal quarters have generally been the highest, with sales during the first fiscal quarter the lowest. This reflects the combined impact of the seasonality of the wholesale and retail segments. Generally, AAI s retail segment has not experienced the same pronounced sales seasonality around the back-to-school and year-end holiday selling seasons as other retailers.

Accounting Pronouncements-Newly Issued

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes-an Interpretation of FASB Statement No. 109 (the Interpretation). The Interpretation establishes for all entities a minimum threshold for financial statement recognition of the benefit of tax positions, and requires certain expanded disclosures. The Interpretation is effective for fiscal years beginning after December 15, 2006, and is to be applied to all open tax years as of the date of effectiveness. The AAI adopted the interpretation as of January 1, 2007 and such adoption did not have a material effect on the AAI s consolidated financial statements (Note 17).

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Adoption is required for fiscal years beginning after November 15,

Table of Contents

2007, and interim periods within those fiscal years. Early adoption of SFAS No. 157 is encouraged. The AAI is currently evaluating the expected effect of SFAS No. 157 on its consolidated financial statements and is currently not yet in a position to determine such effects.

In September 2006, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108 (SAB 108) which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. SAB 108 is effective for fiscal years ending on or after November 15, 2006. The adoption of SAB 108 did not have a material impact on the AAI s consolidated financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption is required for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. AAI is currently evaluating the expected effect of SFAS No. 159 on its consolidated financial statements and is currently not yet in a position to determine such effects.

The FASB ratified the consensuses reached in Emerging Issues Task Force (EITF) Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation) (EITF 06-3). The EITF reached a consensus that the scope of the Issue includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, and may include, but is not limited to, sales, use, value added, and some excise taxes. The presentation of taxes within the scope of this Issue on either a gross or a net basis is an accounting policy decision that should be disclosed. Furthermore, for taxes reported on a gross basis, AAI should disclose the aggregate amount of those taxes in interim and annual financial statements for each period for which an income statement is presented if that amount is significant. The disclosures required under this consensus should be applied retrospectively to interim and annual financial statements for all periods presented, if those amounts are significant. AAI adopted EITF 06-3 on January 1, 2007. The adoption of EITF 06-3 did not have a significant impact on its consolidated financial position or results of operations. AAI currently records its sales net of any value added or sales tax.

All other recently issued accounting pronouncements are not expected to have a material impact on AAI s consolidated financial statements.

Non-GAAP Discussion

In addition to its GAAP results, American Apparel considers non-GAAP measures of its performance. EBITDA, as defined below, is an important supplemental financial measure of American Apparel s performance that is not required by, or presented in accordance with, GAAP.

American Apparel presents EBITDA because it believes it provides an important measure of its financial performance. American Apparel defines EBITDA as net income (loss) before:

- interest expense;
- income taxes; and
- depreciation and amortization.

197

American Apparel s management uses EBITDA as an important financial measure to assess American Apparel s operating performance. American Apparel s management believes that the presentation of EBITDA included in this proxy statement provides a supplementary non-GAAP operating performance measure to assist readers with the overall evaluation of operating performance and also to assist in the review of results of operations for planning and forecasting certain operations in future periods. The presentation also provides a measurement which industry analysts use when evaluating operating performance and to allow comparisons of operating performance to that of competitors. EBITDA will also be useful for calculating bonuses to be paid to management.

Although American Apparel uses EBITDA as a financial measure to assess the performance of its business, there are material limitations to using a measure such as EBITDA, including the difficulty associated with using it as the sole measure to compare the results of one company to another and the inability to analyze significant items that directly affect a company s net income (loss) or operating income because of the following material limitations:

It does not include interest expense. Because AAI borrowed money to finance its operations, interest expense is a necessary and ongoing part of its costs and has assisted in generating revenue. Therefore, any measure that excludes interest has material limitations.

It does not include taxes. Because the payment of taxes is a necessary and ongoing part of operations, any measure that excludes taxes has material limitations.

It does not include depreciation and amortization expense. Because AAI uses capital assets, depreciation and amortization expense is a necessary element of costs and ability to generate revenue. Therefore, any measure that excludes depreciation and amortization expense has material limitations.

American Apparel s management compensates for these limitations in considering EBITDA in conjunction with its analysis of other GAAP financial measures, such as net income (loss).

Since AAI has previously reported non-GAAP segment results to Endeavor s management and the investment community, we believe the inclusion of non-GAAP numbers provides consistency in financial reporting. Lastly, an investor or potential investor may find any one or all these items important in evaluating AAI s performance, its results of operations and financial position. Management compensates for the limitations of using non-GAAP financial measures by using them only to supplement U.S. GAAP results to provide a more complete understanding of the factors and trends affecting AAI s business.

American Apparel had growth in EBITDA of approximately $22.4 million or 124.4% from EBITDA of approximately $18.0 million in the first nine months of 2006 to EBITDA of approximately $40.4 million in the first nine months of 2007.

Reconciliation of AAI s EBITDA

The following table presents a reconciliation of the AAI s EBITDA to its net income (loss) for, the most directly comparable GAAP financial measure, on a historical basis, for the periods presented:

	Nine Months Ended September 30,		Year Ended December 31,				
	2007 (unaudited)	2006 (unaudited)	2006 (unaudited)	2005 (unaudited)	2004 (unaudited)	2003 (unaudited)	2002 (unaudited)
Net income (loss)	$ 11,581	$ (185)	$ (1,624)	$ 3,583	$ 6,323	$ 5,988	$ 1,666
Income taxes	4,725	959	1,335	392	1,019	(379)	13
Interest expense	12,255	7,869	10,797	6,258	1,928	855	671
Depreciation and amortization	8,057	7,299	9,430	5,370	2,206	1,072	478
EBITDA	$ 36,618	$ 15,942	$ 19,938	$ 15,603	$ 11,476	$ 7,536	$ 2,828

198

Table of Contents

Reconciliation of the CI companies EBITDA

The following table presents a reconciliation of the CI companies EBITDA to their net income, the most directly comparable GAAP financial measure, on a historical basis, for the periods presented:

	Nine Months Ended September 30,			
	2007 CDN $ (unaudited)	2007 USD $ (unaudited)	2006 CDN $ (unaudited)	2006 USD $ (unaudited)
Net income	$ 959	$ 871	$ 117	$ 104
Income taxes	812	735	259	228
Interest expense	991	899	803	708
Depreciation and amortization	1,363	1,236	1,181	1,043
EBITDA	$ 4,125	$ 3,741	$ 2,360	$ 2,083

The following table presents a reconciliation of the CI companies EBITDA to their net (loss) income, the most directly comparable GAAP financial measure, on a historical basis, for the periods presented:

	Year Ended December 31,									
	2006 CDN $ (unaudited)	2006 USD $ (unaudited)	2005 CDN $ (unaudited)	2005 USD $ (unaudited)	2004 CDN $ (unaudited)	2004 USD $ (unaudited)	2003 CDN $ (unaudited)	2003 USD $ (unaudited)	2002 CDN $ (unaudited)	2002 USD $ (unaudited)
Net (loss) income	$ (89)	$ (78)	$ (7)	$ (6)	$ 111	$ 85	$ 559	$ 400	$ 225	$ 143
Income taxes	271	239	138	112	71	55	288	206	140	89
Interest expense	1,151	1,014	642	520	343	264	125	90	47	30
Depreciation and amortization	1,611	1,420	1,093	885	378	291	67	48	37	24
EBITDA	$ 2,944	$ 2,595	$ 1,866	$ 1,511	$ 903	$ 695	$ 1,039	$ 744	$ 449	$ 286

Quantitative and Qualitative Disclosures about Market Risk

American Apparel s exposure to market risk is limited to interest rate risk associated with American Apparel s credit facilities and foreign currency exchange risk associated with American Apparel s foreign operations.

Based on AAI s interest rate exposure on variable rate borrowings at September 30, 2007, a one percentage point increase in average interest rates on AAI s borrowings would increase future interest expense by approximately $42 per month. AAI determined these amounts based on approximately $50,359 of variable rate borrowings at September 30, 2007, multiplied this amount by 1% and divided by twelve. AAI is currently not using any interest rate collars or hedges to manage or reduce interest rate risk. As a result, any increase in interest rates on AAI s variable rate borrowings would increase interest expense and reduce net income.

The majority of AAI s operating activities are conducted in US dollars. Approximately 18% of AAI s sales are denominated in other currencies such as Euros, or British Pounds Sterling. Nearly all of AAI s production costs and material costs are denominated in US dollars although the majority of the yarn is sourced from outside the United States. A 10% change in the exchange rate of the US dollar with respect to the foreign countries where the company operates, in a scenario where the US dollar would appreciate against other currencies could have a significant impact on AAI s earnings. We have estimated that for the nine months ended September 30, 2007, such a gain in the value of the US$ would have resulted in a decrease of approximately $3,100 in net income due to the United States being the source for the goods being sold as well as the effect on retail margins which is the primary sales channel in those markets. We have not, however, factored in our ability to raise prices in those markets to compensate for such an increase in the effective cost of our products in foreign markets.

199

Table of Contents

While the CI companies purchases from AAI are denominated in US dollars, its operating activities and all of its sales are denominated in Canadian dollars. A 10% change in the exchange rate of the US dollar with respect to the Canadian dollar, in a scenario where the US dollar would appreciate against the Canadian dollar could have a significant impact on the CI companies earnings. We have estimated that for nine months ended September 30, 2007, such a gain in the value of the US$ would have resulted in a decrease of approximately $1,080 in net income of the CI companies due to the United States being the source for the goods being sold as well as the effect on retail margins which is the primary sales channel for the CI companies. We have not, however, factored in our ability to raise prices in the Canadian market to compensate for such an increase in the effective cost of our products in Canada.

Table of Contents

DIRECTORS AND EXECUTIVE OFFICERS OF ENDEAVOR FOLLOWING THE ACQUISITION

At the effective time of the acquisition, the board of directors and executive officers of Endeavor will be as follows:

Name	Age	Position
Dov Charney	38	Chairman of the Board, Chief executive officer, president and director
Ken Cieply	52	Chief financial officer and treasurer
Robert Greene	48	Director
Mark D. Klein	45	Director
Adrian Kowalewski	29	Director
Allan Mayer	57	Director
Keith Miller	40	Director
Mark Samson	54	Director
Mortimer Singer	30	Director
Mark A. Thornton	42	Director

Directors

Dov Charney is founder of American Apparel and has served as a director, chief executive officer and president of American Apparel since its formation in 1998 and has been a managing member of LLC since its formation in 1998. Prior to starting American Apparel, Mr. Charney founded American Heavy, Inc., an apparel company located in Columbia, South Carolina, in 1989, and served as its founder and chief executive officer until 1996. Mr. Charney is a graduate of Choate Rosemary Hall and attended Tufts University.

Ken Cieply has been the chief financial officer of American Apparel since June 2006, overseeing the domestic and international financial and administrative activities for the company. Prior to joining American Apparel, Mr. Cieply worked as an independent business and financial consultant in Montreal, Canada from May 2004 to June 2006. From 2000 to May 2004, he was vice president of finance and chief financial officer of Cavalier Specialty Yarn Inc., a manufacturer with locations in Canada and the United States. From 1999 to 2000, Mr. Cieply was executive vice president and chief financial officer of Grand Toys International Inc., a Nasdaq-listed distributor and licensee of toys in Canada and the United States. Prior to Grand Toys, he served from 1994 to 1999 as vice president of finance and administration for Gildan Activewear Inc., a publicly-traded manufacturer and distributor of active wear with locations in Canada, the United States, Central America and the Caribbean. Mr. Cieply successfully led that company s 1998 initial public offering on U.S. and Canadian public markets. Prior to joining Gildan, Mr. Cieply was vice president of finance for Rosilco International, a manufacturer and importer of textiles based in Montreal, from 1988 to 1994. Mr. Cieply previously served as controller of several companies between 1981 and 1988. He began his career as an accountant at KPMG. Mr. Cieply holds a Bachelor of Commerce degree from McGill University and is a member of the Canadian Institute of Chartered Accountants.

Robert Greene will become a director of Endeavor upon consummation of the acquisition of American Apparel. Mr. Greene is a bestselling author known for his books on strategy. Mr. Greene has worked as a private consultant to several executives in businesses ranging from financial management, to artists agencies and film producers. He has written three books, all published by Penguin: The 48 Laws of Power (1998, over 900,000 copies sold in US, and translated into 21 languages); The Art of Seduction (2001) and The 33 Strategies of War (2006). He has worked in New York City as an editor and writer for several magazines, including Esquire, and in Hollywood as a story developer and writer. He lived for years in London, England; Paris, France; and Barcelona, Spain; he speaks several languages and has worked as a translator. He attended the University of California, Berkeley and the University of Wisconsin-Madison, where he received a B.A. in classical studies.

Mark D. Klein will become a director of Endeavor upon consummation of the acquisition of American Apparel. Mr. Klein has been Chief Executive Officer, President and a Director of Alternative Asset Management

Acquisition Corp., a publicly traded blank check company formed for the purpose of acquiring an operating business, since February 2007. Mr. Klein is presently the Chief Executive Officer of Hanover Group US LLC, a newly formed indirect US subsidiary of the Hanover Group, whose primary purpose is to be involved with the organization and initial public offering of a blank check company. Mr. Klein is also an investment banker at Ladenburg Thalmann & Co. Inc. and a Managing Member of the LTAM Titan Fund, a fund of funds hedge fund. Prior to joining Hanover in 2007, Mr. Klein was Chairman of Ladenburg Thalmann & Co., Inc., a leading underwriter of blank check companies, which is engaged in retail and institutional securities brokerage, investment banking and asset management services. From March 2005 to September 2006, he was Chief Executive Officer and President of Ladenburg Thalmann Financial Services, Inc., the parent of Ladenburg Thalmann & Co., Inc., and Chief Executive Officer of Ladenburg Thalmann Asset Management Inc., a subsidiary of Ladenburg Financial Services, Inc. Prior to joining Ladenburg Thalmann, from June 2000 to March 2005 Mr. Klein served as the Chief Executive Officer and President of NBGI Asset Management, Inc. and NBGI Securities, which were the US subsidiaries of the National Bank of Greece, the largest financial institution in Greece. Prior to joining NBGI, Mr. Klein was President and Founder of Newbrook Capital Management, and Founder and Managing Member of Independence Holdings Partners, LLC, a private equity fund of funds company. Prior to the formation of Newbrook Capital Management and Independence Holdings Partners, LLC, Mr. Klein was a Senior Portfolio Manager for PaineWebber and Smith Barney Shearson. Prior to his affiliation with PaineWebber and Smith Barney Shearson, Mr. Klein managed investment accounts at Prudential Securities and managed firm capital at MKI Securities. Before entering the securities industry, Mr. Klein worked for two years at Arthur Young in its Entrepreneurial Services Group. Mr. Klein is a graduate of J.L. Kellogg Graduate School of Management at Northwestern University, with a Masters of Management Degree and also received a Bachelors of Business Administration degree with high distinction from Emory University.

Adrian Kowalewski will become a director of Endeavor upon consummation of the acquisition of American Apparel. Mr. Kowalewski has been with American Apparel since June 2006. In his role as Director of Corporate Finance & Development, he has been chiefly involved in the corporate finance function and helping set company strategy. From July 1999 to June 2002, he worked in the Mergers & Acquisitions Group of CIBC World Markets in New York and London, where he was involved in advising public and private companies in North America and Europe on mergers and acquisition transactions. From July 2003 to July 2004, he worked for Houlihan Lokey Howard & Zukin, where he participated in financial restructurings, mergers and acquisitions, and private placements. He also worked at Lazard Freres & Co., a preeminent advisory investment bank. Mr. Kowalewski holds an A.B. with honors from Harvard University, and an M.B.A. from the University of Chicago Graduate School of Business.

Allan Mayer will become a director of Endeavor upon consummation of the acquisition of American Apparel. Since October 2006, he has been a principal partner, member of the management committee, and head of the Strategic Communications Division of 42West LLC, a leading public relations firm. In this capacity, and in his previous position as managing director and head of the entertainment practice at the nationally-known crisis communications firm Sitrick And Company, which he held from 1997 until October 2006, he has advised a wide range of corporate and institutional clients in the entertainment and related industries, including, among others, Imagine Entertainment, the Los Angeles Dodgers, the Major League Baseball Players Association, the Motion Picture Association of America, MTV Networks, the Recording Industry Association of America, Sony Pictures, United Artists, Universal Studios, and The Weinstein Co., as well as providing strategic counsel to such high-profile individuals as Halle Berry, Jim Carrey, Tom Cruise, Johnny Depp, Eminem, Brian Grazer, Ron Howard, Rush Limbaugh, and Steven Spielberg. Mr. Mayer served as a staff reporter for *The Wall Street Journal* from 1972 to 1973; a writer, foreign correspondent and senior editor for *Newsweek* from 1973 to 1982, and the founding editor (and later publisher) of *Buzz* magazine from 1990 to 1997. He served as editorial director of Arbor House Publishing Co. from 1987 to 1988 and senior editor of Simon & Schuster from 1988 to 1990. Mr. Mayer has authored two books *Madam Prime Minister: Margaret Thatcher and Her Rise to Power* (Newsweek Books, 1980) and *Gaston s War* (Presidio Press, 1987). He also is co-author, with Michael S. Sitrick, of *Spin: How To Turn The Power of the Press to Your Advantage* (Regnery, 1998). In addition, he has written for a wide variety of national publications, ranging from *The New York Times Magazine* to *Vogue*. Mr. Mayer is a

Table of Contents

recipient of numerous professional honors, including the National Magazine Award, the Overseas Press Club Citation of Excellence, and six William Allen White Awards. Mr. Mayer serves on the Board of Directors of Film Independent and lectures regularly on crisis management and communications at UCLA s Anderson School of Business and USC s Annenberg School of Communication. Mr. Mayer received his B.A. from Cornell University.

Keith Miller is a partner of Goode Consumer Advisors. Prior to joining Goode at it s formation in January 2006, Mr. Miller was a private investor and advisor to the global consumer branded marketplace. From October 2002 to March 2006, Mr. Miller served as a senior advisor to Itochu Corporation s executive management in Osaka and Tokyo, Japan. His responsibilities included the origination, structuring and the execution of brand related mergers and acquisitions, licenses, distribution and joint venture agreements in Asia. As a principal investor and while assisting Itochu, Mr. Miller targeted the acquisition of many consumer and lifestyle brands with global awareness and positioning. From 1987 to 1999, Mr. Miller was the co-founder and President of a manufacturing business which supplied some of the most notable brands in the world including: Gap, Adidas, Old Navy, Polo Ralph Lauren, Levi Strauss and Company, Express, and The Limited. Mr. Miller is an advisory board member and shareholder of Chrome Hearts, Inc., and advisory board member to LeSportsac, Shabby Chic, Intermix, Vestal Watch Company and James Perse. Mr. Miller sits on the board of the Sachdev Group of New Dehli, India which operates and manages global luxury consumer brands in the country of India. Mr. Miller continues to advise many well known entrepreneurs, CEOs and principal shareholders in the consumer marketplace.

Mark Samson will become a director of Endeavor upon consummation of the acquisition of American Apparel. Since 1999, Mr. Samson has been Managing Director of Getzler Henrich and Associates LLC., a leading corporate restructuring firm in the U.S. with a focus on middle market companies. In this capacity, he has served as interim chief executive officer, chief operating officer and/or chief restructuring officer and financial advisor for more than 40 companies. During his tenure with Getzler Henrich, Mr. Samson has provided numerous clients with guidance in operational restructuring, bankruptcy proceedings and business operation, management practices, cash flow and profitability improvements. From 1984 to 2000, Mr. Samson served as Executive Chairman of the Board, Co-President and Chief Executive Officer of Debjon Group/Sidcor/MQM Group, a consortium of 53 vertically integrated retail businesses and convenience stores. From 1976 to 1984, Mr. Samson was Marketing Director for the Berden Group, the largest manufacturer of work wear and corporate uniforms in Africa. Mr. Samson received his BBA in Economics and Marketing from the University of South Africa and is a member of the Turnaround Management Association and American Bankruptcy Institute.

Mortimer Singer will become a director of Endeavor upon consummation of the acquisition of American Apparel. Mr. Singer has been a Senior Vice President of Marvin Traub Associates (MTA), a business development and strategy consulting firm focused on working with brands, retailers, developers and related businesses that operate in the retail and consumer goods sectors, since April 2003. In this capacity he oversees all aspects of MTA s business, from merger and acquisition advisory services to strategic consulting in the fashion and retail industries for clients in the U.S., as well as Russia, India, Europe and other locales. In this capacity he also co-founded and became Managing Director of Traub Singer Magnusdottir Capital, MTA s venture division. Prior to joining MTA, Mr. Singer launched, in August 2002, the U.S. division of Quintessentially, a UK based luxury concierge services, where he headed the sale and business development initiative, as well as US brand development until April 2003. From June 2000 to June 2002, Mr. Singer worked in the Technology, Media and Telecom division of JPMorgan Chase, where he advised domestic clients on acquisitions, divestitures, restructurings, joint ventures and financing alternatives. He received his BA from the University of Pennsylvania.

Mark A. Thornton will become a director of Endeavor upon consummation of the acquisition of American Apparel. Since January 2005, Mr. Thornton has been an independent consultant to various clients, advising them in the areas of private equity raises and project management, and also lectures at the Harvard Negotiation Insight Initiative. From April 2002 until December 2004, Mr. Thornton researched and authored a book, entitled *Meditation in a New York Minute,* which was published by Sounds True. At various times during the period from

1997 to March 2002, Mr. Thornton worked in several capacities for JPMorgan, including serving as the Chief Operating Officer for JPMorgan Private Bank in London from June 2001 to March 2002, specializing in operational risk management relating to the merger of JPMorgan with Robert Fleming. He oversaw core aspects of the merger and chaired numerous committees related to operational risk, new product lines and new business development. Prior to joining JPMorgan in 1997, Mr. Thornton worked in various market risk and credit risk positions for blue chip investment banks and securities firms, including Daiwa Europe Bank plc and Australian and New Zealand Banking Group Ltd.

Compensation of Directors

Our non-employee directors will receive annual stock grants equal to that number of shares of our common stock having an aggregate market value of $75,000 at the time of grant, with grants being made at the closing of the proposed acquisition and on each anniversary of service thereafter. Non-employee directors also will receive $1,000 for each board and committee meeting attended and shall be reimbursed for travel expenses incurred in connection with attending these meetings.

The following table sets forth certain information regarding the benefits to be provided with respect to such grants to the extent reasonably anticipated on the reflected on November 16, 2007, the record date, and reflects only grants proposed to made on the date of closing of the acquisition.

Name and Position		Value of Grant
Chief Executive Officer		
Dov Charney	$	0
Non-employee Directors		
Robert Greene	$	75,000
Mark D. Klein	$	75,000
Allan Mayer	$	75,000
Keith Miller	$	75,000
Mark Samson	$	75,000
Mortimer Singer	$	75,000
Mark A. Thornton	$	75,000
All Executive Officers	$	0
All Non-employee Directors	$	525,000
All Non-executive Officers and Employees	$	0

Meetings and Committees of the Board of Directors of Endeavor

During the fiscal year ended December 31, 2006, Endeavor s board of directors held five meetings. Although Endeavor does not have any formal policy regarding director attendance at annual stockholder meetings, Endeavor will attempt to schedule its annual meetings so that all of its directors can attend. Endeavor expects its directors to attend all board and committee meetings and to spend the time needed and meet as frequently as necessary to properly discharge their responsibilities.

Independence of Directors

Endeavor will adhere to the rules of the American Stock Exchange in determining whether a director is independent. The board of directors of Endeavor also will consult with Endeavor s counsel to ensure that the board s determinations are consistent with those rules and all relevant securities and other laws and regulations regarding the independence of directors. The American Stock Exchange listing standards define an independent director generally as a person, other than an officer of a company, who does not have a relationship with the company that would interfere with the director s exercise of independent judgment. Consistent with these

Table of Contents

considerations, the board of directors of Endeavor has affirmatively determined that, upon appointment to the board of directors of Endeavor on the closing of the acquisition, Messrs. Greene, Klein, Mayer, Miller, Samson, Singer and Thornton will be the independent directors of Endeavor.

Audit Committee

Effective December 21, 2005, Endeavor established an audit committee of the board of directors, which consists of Edward J. Mathias, as chairman, Jay H. Nussbaum and Richard Y. Roberts, each of whom is an independent director under the American Stock Exchange s listing standards. Following the consummation of the acquisition, the members of the audit committee will be Messrs. Klein, Samson and Thornton, with Mr. Klein as Chairman.

The audit committee s duties, which are specified in our Audit Committee Charter, include, but are not limited to:

- reviewing and discussing with management and the independent auditor the annual audited financial statements, and recommending to the board whether the audited financial statements should be included in our Form 10-K;

- discussing with management and the independent auditor significant financial reporting issues and judgments made in connection with the preparation of our financial statements;

- discussing with management and the independent auditor the effect on our financial statements of (i) regulatory and accounting initiatives and (ii) off-balance sheet structures;

- discussing with management major financial risk exposures and the steps management has taken to monitor and control such exposures, including our risk assessment and risk management policies;

- reviewing disclosures made to the audit committee by our principal executive officer and principal financial officer during their certification process for our Form 10-Ks and Form 10-Qs about any significant deficiencies in the design or operation of internal controls or material weaknesses therein and any fraud involving management or other employees who have a significant role in our internal controls;

- verifying the rotation of the lead (or coordinating) audit partner having primary responsibility for the audit and the audit partner responsible for reviewing the audit as required by law;

- reviewing and approving all related-party transactions including analyzing the shareholder base of each target business so as to ensure that we do not consummate a business combination with an entity that is affiliated with our management;

- inquiring and discussing with management our compliance with applicable laws and regulations;

- pre-approving all audit services and permitted non-audit services to be performed by our independent auditor, including the fees and terms of the services to be performed;

- appointing or replacing the independent auditor;

reviewing proxy disclosure to ensure that it is in compliance with SEC rules and regulations;

determining the compensation and oversight of the work of the independent auditor (including resolution of disagreements between management and the independent auditor regarding financial reporting) for the purpose of preparing or issuing an audit report or related work; and

establishing procedures for the receipt, retention and treatment of complaints received by us regarding accounting, internal accounting controls or reports which raise material issues regarding our financial statements or accounting policies.

Table of Contents

Financial Experts on Audit Committee

The audit committee will at all times be composed exclusively of independent directors who are financially literate as defined under the American Stock Exchange s listing standards. The American Stock Exchange s listing standards define financially literate as being able to read and understand fundamental financial statements, including a company s balance sheet, income statement and cash flow statement.

In addition, we must certify to the American Stock Exchange that the committee has, and will continue to have, at least one member who has past employment experience in finance or accounting, requisite professional certification in accounting, or other comparable experience or background that results in the individual s financial sophistication. The board of directors has determined that Edward J. Mathias currently satisfies, and upon consummation of the acquisition, Mr. Samson will satisfy, the American Stock Exchange s definition of financial sophistication and also qualifies as an audit committee financial expert, as defined under rules and regulations of the SEC.

Auditor Fees

The firm of Marcum & Kliegman LLP acts as Endeavor s independent registered public accounting firm. The following is a summary of fees paid by Endeavor to Marcum & Kliegman LLP for services rendered.

Audit Fees

During the fiscal year ended December 31, 2006, audit fees for Endeavor s independent registered public accounting firm were $37,000.

During the period from July 22, 2005 (inception) to December 31, 2005, fees for Endeavor s independent registered public accounting firm were $70,000 for the services they performed in connection with Endeavor s IPO, including the financial statements included in the Form 8-K filed with the SEC on December 21, 2005 and the audit of Endeavor s December 31, 2005 Annual Report on Form 10-K.

Audit Related Fees

During 2006, Endeavor s independent registered public accounting firm rendered audit related services amounting to $14,000 related to the American Apparel transaction.

Tax Fees

During 2006, Endeavor s independent registered public accounting firm rendered services to Endeavor for tax compliance, tax advice and tax planning in the amount of $3,500.

All Other Fees

During 2005 and 2006, there were no fees billed for products and services provided by Endeavor s independent registered public accounting firm other than those set forth above.

Audit Committee Approval

Since Endeavor s audit committee was not formed until December 2005, the audit committee did not pre-approve all of the foregoing services although any services rendered prior to the formation of Endeavor s audit committee were approved by Endeavor s board of directors. However, in accordance with Section 10A(i) of the Securities Exchange Act of 1934, before Endeavor engages its independent accountant to render audit or non-audit services on a going-forward basis, the engagement will be approved by our audit committee.

Code of Ethics

In December 2005, our board of directors adopted a code of ethics that applies to our directors, officers and employees as well as those of our subsidiaries. Requests for copies of our code of ethics should be sent in writing to Endeavor Acquisition Corp., 590 Madison Avenue, 21st Floor, New York, New York 10022.

Compensation Committee Information

Upon consummation of the acquisition, the board of directors of Endeavor will establish a compensation committee with Messrs. Greene, Mayer, Miller, Singer and Thornton as its initial members, each an independent director under the American Stock Exchange s listing requirements, with Mr. Miller as Chairman. The purpose of the compensation committee will be to review and approve compensation paid to Endeavor s officers and to administer American Apparel s incentive compensation plans, including authority to make and modify awards under such plans. Initially, the only plan will be the 2007 performance equity plan.

Nominating Committee Information

Nominating Committee

Effective December 2005, Endeavor established a nominating committee of the board of directors, which consists of Kerry Kennedy, as chairman, and Robert B. Hersov, each of whom is an independent director under the American Stock Exchange s listing standards. Following the acquisition, the members will be Messrs. Miller, Singer and Greene, each an independent director under the American Stock Exchange s listing standards, as well as Mr. Charney, with Mr. Singer as Chairman.

The nominating committee is responsible for overseeing the selection of persons to be nominated to serve on our board of directors. The nominating committee considers persons identified by its members, management, shareholders, investment bankers and others. The guidelines for selecting nominees, which are specified in the Nominating Committee Charter, generally provide that persons to be nominated should be actively engaged in business endeavors, have an understanding of financial statements, corporate budgeting and capital structure, be familiar with the requirements of a publicly traded company, be familiar with industries relevant to our business endeavors, be willing to devote significant time to the oversight duties of the board of directors of a public company, and be able to promote a diversity of views based on the person s education, experience and professional employment. The nominating committee evaluates each individual in the context of the board as a whole, with the objective of recommending a group of persons that can best implement our business plan, perpetuate our business and represent shareholder interests. The nominating committee may require certain skills or attributes, such as financial or accounting experience, to meet specific board needs that arise from time to time. The nominating committee does not distinguish among nominees recommended by shareholders and other persons.

There have been no material changes to the procedures by which security holders may recommend nominees to our board of directors.

Election of Directors; Voting Agreement

The Endeavor Inside Stockholders and Mr. Charney will enter into a voting agreement at closing of the acquisition. The voting agreement will provide that Mr. Charney, on the one hand, and such Endeavor Inside Stockholders, on the other hand, will each designate four directors and mutually designate one additional directors to Endeavor s board. Each of the parties to the voting agreement will vote for such designees as directors of Endeavor until immediately following the election that will be held in 2010. Endeavor will be obligated to have a board of directors comprised of nine members and to enable the election to the board of directors of the persons designated by the parties to the voting agreement. The voting agreement is attached to this proxy statement as *Annex E*. We encourage you to read the voting agreement in its entirety.

Table of Contents

Immediately upon the consummation of the acquisition, the directors of Endeavor will be Messrs. Charney, Greene, Klein, Kowalewski, Mayer, Miller, Samson, Singer and Thornton. Under the terms of the voting agreement, Mr. Charney, on the one hand, and the Endeavor Inside Stockholders who are party to the voting agreement, on the other hand, have agreed to vote for the designees to Endeavor s board of directors through the election in 2010 as follows:

in the class to stand for reelection in 2008 Messrs. Greene, Miller and Mayer.

in the class to stand for reelection in 2009 Messrs. Kowalewski, Klein and Singer.

in the class to stand for reelection in 2010 Messrs. Charney, Samson and Thornton.

Endeavor s directors do not currently receive any cash compensation for their services as members of the board of directors. Our non-employee directors will receive annual stock option grants to purchase that number of shares of our common stock having an aggregate market value of $75,000 at the time of grant, with grants being made at the closing of the proposed acquisition and on each anniversary of service thereafter. See the section entitled *2007 Performance Equity Plan Proposal Background.* Non-employee directors also will receive $1,000 for each board and committee meeting attended and shall be reimbursed for travel expenses incurred in connection with attending these meetings.

Executive Officers

As previously stated, Mr. Charney shall serve as chief executive officer and president of Endeavor and Ken Cieply shall serve as Chief Financial Officer following the consummation of the acquisition. In addition, following the closing, the board of directors of Endeavor may, in the normal course of its duties, in consultation with the chief executive officer, elect one or more individuals to serve the company as chief operating officer and chief information officer. It is currently anticipated that the successful candidate for each of these positions shall be familiar with the corporate responsibilities and obligations of officers of public companies, to shareholders, customers and the public. Further, it is currently anticipated that American Apparel s current officers and employees (other than Mr. Lim) will continue in the same or substantially the same capacities with American Apparel after the acquisition.

Executive Compensation

No executive officer of Endeavor has received any cash or non-cash compensation for services rendered to Endeavor. Each executive officer has agreed not to take any compensation prior to the consummation of a business combination.

From inception through January 1, 2007, Endeavor paid $7,500 per month to Ironbound Partners Fund, LLC, for general and administrative services. Ironbound is an affiliate of Jonathan Ledecky, Endeavor s president and secretary. This arrangement ceased as of January 1, 2007. From January 1, 2007 through April 2007, Endeavor paid a monthly rental of $3,000 for office space to an unaffiliated party. Endeavor was not required to pay any rent for space during from May 2007 through October 2007. Commencing November 1, 2007 Endeavor is required to pay a monthly rental of $2,500 to another unaffiliated party for office space for the benefit of their consultants. Other than the aforementioned fee paid to Ironbound, no compensation of any kind, including finders and consulting fees, have been or will be paid to any of Endeavor s officers for services rendered prior to the closing of the acquisition. However, Endeavor s executive officers are reimbursed for any out-of-pocket expenses incurred in connection with activities on Endeavor s behalf such as identifying potential target business and performing due diligence on suitable business combinations. As of the record date, an aggregate of approximately $254,000 has been reimbursed to them for such expenses.

Upon consummation of the acquisition, Endeavor will operate in the retail apparel industry. In connection with the acquisition of American Apparel, Endeavor will enter into an employment agreement with Mr. Charney for him to serve as Endeavor s chief executive officer. It also is anticipated that Endeavor will hire and enter into employment agreements with a chief financial officer, chief operating officer and a chief information officer.

Table of Contents

The policies of Endeavor with respect to the compensation of the aforementioned executive officers and other executive officers following the acquisition will be administered by Endeavor s board in consultation with its compensation committee. This committee will be formed from the independent directors on Endeavor s board following consummation of the acquisition. Messrs. Greene, Miller, Mayer, Singer and Thornton shall serve as its members. Mr. Miller will be the initial chairperson of this committee. The compensation policies followed by Endeavor will be intended to provide for compensation that is sufficient to attract, motivate and retain executives of outstanding ability and potential and to establish an appropriate relationship between executive compensation and the creation of shareholder value. To meet these goals, the compensation committee will be charged with recommending executive compensation packages to Endeavor s board of directors.

It is anticipated that performance-based and equity-based compensation will be an important foundation in executive compensation packages as Endeavor believes it is important to maintain a strong link between executive incentives and the creation of shareholder value. Endeavor believes that performance and equity-based compensation can be an important component of the total executive compensation package for maximizing shareholder value while, at the same time, attracting, motivating and retaining high-quality executives. The employment agreements to be entered into by future executive officers of Endeavor and the adoption of the proposed 2007 performance equity plan reflect and will reflect what Endeavor believes is a focus on performance- and equity-based compensation. Since Endeavor will not have a compensation committee until completion of the acquisition, Endeavor has not yet adopted any formal guidelines for allocating total compensation between equity compensation and cash compensation for executives hired in the future.

Compensation Discussion and Analysis

Overall, Endeavor will seek to provide total compensation packages that are competitive in terms of potential value to its executives, and which are tailored to the unique characteristics and needs of Endeavor within its industry in order to create an executive compensation program that will adequately reward its executives for their roles in creating value for Endeavor shareholders. Endeavor intends to be competitive with other similarly situated companies in its industry following completion of the acquisition.

The compensation decisions regarding Endeavor s executives will be based on Endeavor s need to attract individuals with the skills necessary for Endeavor to achieve its business plan, to reward those individuals fairly over time, and to retain those individuals who continue to perform at or above Endeavor s expectations.

It is anticipated that Endeavor s executives compensation will have three primary components salary, cash incentive bonus and stock-based awards. Endeavor will view the three components of executive compensation as related but distinct. Although Endeavor s compensation committee will review total compensation, Endeavor does not believe that significant compensation derived from one component of

compensation should negate or reduce compensation from other components. Endeavor anticipates determining the appropriate level for each compensation component based in part, but not exclusively, on its view of internal equity and consistency, individual performance and other information deemed relevant and timely. Since Endeavor s compensation committee will not be formed until consummation of the acquisition, Endeavor has not adopted any formal or informal policies or guidelines for allocating compensation between long-term and currently paid out compensation, between cash and non-cash compensation, or among different forms of compensation.

In addition to the guidance provided by its compensation committee, Endeavor may utilize the services of third parties from time to time in connection with the hiring and compensation awarded to executive employees. This could include subscriptions to executive compensation surveys and other databases.

Endeavor s compensation committee will be charged with performing an annual review of Endeavor s executive officers cash compensation and equity holdings to determine whether they provide adequate incentives and motivation to executive officers and whether they adequately compensate the executive officers relative to comparable officers in other companies.

Table of Contents

Benchmarking of Cash and Equity Compensation

Endeavor believes it is important when making compensation-related decisions to be informed as to current practices of similarly situated publicly held companies in the apparel industries. Endeavor expects that the compensation committee will stay apprised of the cash and equity compensation practices of publicly held companies in the apparel and related industries through the review of such companies public reports and through other resources. It is expected that any companies chosen for inclusion in any benchmarking group would have business characteristics comparable to Endeavor, including revenues, financial growth metrics, stage of development, employee headcount and market capitalization. While benchmarking may not always be appropriate as a stand-alone tool for setting compensation due to the aspects of Endeavor post-acquisition business and objectives that may be unique to Endeavor, Endeavor generally believes that gathering this information will be an important part of its compensation-related decision-making process.

Compensation Components

Base Salary. Generally, Endeavor, working with the compensation committee, anticipates setting executive base salaries at levels comparable with those of executives in similar positions and with similar responsibilities at comparable companies. Endeavor will seek to maintain base salary amounts at or near the industry norms while avoiding paying amounts in excess of what Endeavor believes is necessary to motivate executives to meet corporate goals. It is anticipated base salaries will generally be reviewed annually, subject to terms of employment agreements, and that the compensation committee and board will seek to adjust base salary amounts to realign such salaries with industry norms after taking into account individual responsibilities, performance and experience.

Annual Bonuses. Endeavor intends to utilize cash incentive bonuses for executives to focus them on achieving key operational and financial objectives within a yearly time horizon. Near the beginning of each year, the board, upon the recommendation of the compensation committee and subject to any applicable employment agreements, will determine performance parameters for appropriate executives. At the end of each year, the board and compensation committee will determine the level of achievement for each corporate goal.

The performance parameters for which executive officers are eligible to receive cash bonuses under the terms of the employment agreements to be executed in connection with the consummation of the acquisition will be set by the compensation committee each year, within 45 days of approval of such year s annual budget.

Endeavor will structure cash incentive bonus compensation so that it is taxable to its employees at the time it becomes available to them.

Section 162(m). At this time, it is anticipated that one or more executive officer s annual cash compensation may exceed $1 million, and Endeavor has accordingly made any plans to qualify for any compensation deductions under Section 162(m) of the Code. With some exceptions, Section 162(m) of the federal income tax laws will limit Endeavor s deduction for compensation in excess of $1 million paid to certain covered employees (generally the Chief Executive Officer and four next highest-paid executive officers). Compensation paid to covered employees is not subject to the deduction limitation if it is considered qualified performance-based compensation within the meaning of Section 162(m) of the Code. The compensation committee shall reserve the discretion to provide compensation that is both market and performance-based. While it is anticipated that the compensation committee will consider the tax impact of any compensation arrangement, the compensation committee will evaluate such impact in light of Endeavor s overall compensation objectives. The compensation committee will have the right to approve non-deductible compensation if the compensation committee believes it is in the best interests of Endeavor shareholders.

Equity Awards. Endeavor also will use stock options and other stock-based awards to reward long-term performance. Endeavor believes that providing a meaningful portion of its executives total compensation package in stock options and other stock-based awards will align the incentives of its executives with the

Table of Contents

interests of Endeavor s shareholders and with Endeavor s long-term success. The compensation committee and board will develop their equity award determinations based on their judgments as to whether the complete compensation packages provided to Endeavor s executives, including prior equity awards, are sufficient to retain, motivate and adequately award the executives.

Equity awards will be granted through Endeavor s 2007 performance equity plan, which was adopted by Endeavor board and is being submitted to the stockholder of Endeavor for their consideration at the special meeting. All of Endeavor s employees, directors, officers and consultants will be eligible to participate in the 2007 performance equity plan. The material terms of the 2007 Performance Equity Plan are further described in the section of this proxy statement entitled 2007 performance equity plan Proposal. No awards have been made under the plan as of the date of this proxy statement. It is anticipated that all options granted under the plan in the future will have an exercise price at least equal to the fair market of Endeavor s common stock on the date of grant.

Endeavor will account for any equity compensation expense under the rules of SFAS 123R, which requires a company to estimate and record an expense for each award of equity compensation over the service period of the award. Accounting rules also will require Endeavor to record cash compensation as an expense at the time the obligation is accrued. Until Endeavor achieves sustained profitability, the availability to it of a tax deduction for compensation expense is not material to its financial position.

Severance Benefits. Endeavor currently has no severance benefits plan. Endeavor may consider the adoption of a severance plan for executive officers and other employee in the future. The employment agreements to be entered into by the persons who will initially serve as executive officers of Endeavor following consummation of the acquisition provide fore certain rights and obligations in the event of the termination of employment as more fully described in the section of this proxy statement entitled Employment Agreements.

Other Compensation. Endeavor will establish and maintain various employee benefit plans, including medical, dental, life insurance and 401(k) plans. These plans will be available to all salaried employees and will not discriminate in favor of executive officers. Endeavor may extend other perquisites to its executives that are not available to our employees generally.

Employment Agreement and Non-Competition Covenants

In connection with the consummation of the acquisition, Mr. Charney will enter into a three year employment agreement with Endeavor. Under the terms of the employment agreement, Mr. Charney will serve full-time as the chief executive officer of Endeavor and American Apparel for an initial term of three years. The employment agreement provides that Mr. Charney will receive an annual base salary of $750,000. Mr. Charney also will be eligible to receive an annual bonus of 150% of his base salary upon the attainment by Endeavor of performance criteria to be established by its compensation committee as soon as practicable after consummation of the acquisition. Mr. Charney also will be eligible to receive a long-term bonus of 300% of his base salary upon the attainment by Endeavor of long-term performance criteria over the three-year term of this agreement, as established by the compensation committee as soon as practicable after consummation of the acquisition.

Each of Messrs. Charney and Lim has agreed in the Acquisition Agreement to refrain from competing with Endeavor or American Apparel or soliciting their respective employees or customers for a period of four years from the closing of the acquisition.

Table of Contents

BENEFICIAL OWNERSHIP OF SECURITIES

Security Ownership of Certain Beneficial Owners and Management

The following tables set forth information regarding the beneficial ownership of Endeavor s common stock as of the record date, November 16, 2007, and after consummation of the acquisition by:

- each person known by us to be the beneficial owner of more than 5% of Endeavor s outstanding shares of common stock either on the record date or after the consummation of the acquisition;
- each of Endeavor s current executive officers and directors;
- each person who will become director upon consummation of the acquisition;
- all Endeavor s current executive officers and directors as a group; and
- all of Endeavor s executive officers and directors as a group after the consummation of the acquisition.

The following table shows beneficial ownership after the consummation of the acquisition if (i) none of the shares of common stock sold in Endeavor s initial public offering are converted and (ii) 19.99% of the shares of common stock sold in Endeavor s initial public offering are converted:

	Beneficial Ownership of Endeavor Common Stock on November 16, 2007		Beneficial Ownership of Endeavor Common Stock after Acquisition Consummation Assuming Maximum Conversions		Beneficial Ownership of Endeavor Common Stock after Acquisition Consummation Assuming no Conversions	
Name and Address of Beneficial Owner (1)	**Number of Shares**	**Percent of Class before Acquisition**	**Number of Shares**	**Percent of Class after Acquisition**	**Number of Shares**	**Percent of Class after Acquisition**
Jonathan J. Ledecky	1,775,000	8.9%	1,775,000	3.6%	1,775,000	3.4%
Eric J. Watson	1,775,000 (2)	8.9%	1,775,000 (2)	3.6%	1,775,000 (2)	3.4%
Jay H. Nussbaum	40,000	*	40,000	*	40,000	*
Kerry Kennedy (3)	40,000	*	40,000	*	40,000	*
Robert B. Hersov (4)	40,000	*	40,000	*	40,000	*
Edward J. Mathias (5)	40,000	*	40,000	*	40,000	*
Richard Y. Roberts (6)	40,000	*	40,000	*	40,000	*

T. Rowe Price Associates, Inc. (7)	1,557,600 (8)	7.8%	1,557,600 (8)	3.2%	1,557,600 (8)	3.0%
JLF Asset Management, L.L.C. (9)	1,027,467 (10)	5.2%	1,027,467 (10)	2.1%	1,027,467 (10)	2.0%
Fir Tree, Inc. (11)	1,964,200 (11)	9.9%	1,964,200 (11)	4.0%	1,964,200 (11)	3.8%
Prentice Capital Management, LP (13)	1,000,000 (14)	5.0%	1,000,000 (14)	2.0%	1,000,000 (14)	1.9%
Steven A. Cohen (15)	1,751,550 (16)	8.7%	1,751,550 (16)	3.6%	1,751,550 (16)	3.4%
Gilder, Gagnon, Howe & Co. LLC (17)	1,082,043 (18)	5.4%	1,082,043 (18)	2.2%	1,082,043 (18)	2.1%
FMR Corp. (19)	2,709,133 (20)	13.6%	2,709,133 (20)	5.5%	2,709,133 (20)	5.2%
Morgan Stanley (21)	2,885,652 (22)	13.6%	2,885,652 (22)	5.5%	2,885,625 (22)	5.2%
Fred Alger Management, Inc. (23)	2,342,000 (24)	11.6%	2,342,000	4.8%	2,342,000	4.5%
Scott A. Bommer (25)	1,165,000 (26)	5.9%	1,165,000	2.4%	1,165,000	2.2%
Weiss Multi-Strategy Advisors LLC et al (27)	1,010,000 (28)	5.1%	1,010,000	2.2%	1,010,000	2.0%
Dov Charney (29)	*	*	37,258,065	69.1%	37,258,065	65.2%
Robert Greene (29)	*	*	*	*	*	*
Mark D. Klein (29)	*	*	*	*	*	*
Adrian Kowalewski (29)	*	*	*	*	*	*
Allan Mayer (29)	*	*	*	*	*	*
Keith Miller (29)	*	*	*	*	*	*
Mark Samson (29)	*	*	*	*	*	*
Mortimer Singer (29)	*	*	*	*	*	*
Mark A. Thornton (29)	*	*	*	*	*	*

212

Table of Contents

	Beneficial Ownership of Endeavor Common Stock on September 24, 2007		Beneficial Ownership of Endeavor Common Stock after Acquisition Consummation Assuming Maximum Conversions		Beneficial Ownership of Endeavor Common Stock after Acquisition Consummation Assuming no Conversions	
Name and Address of Beneficial Owner (1)	**Number of Shares**	**Percent of Class before Acquisition**	**Number of Shares**	**Percent of Class after Acquisition**	**Number of Shares**	**Percent of Class after Acquisition**
Chief financial officer	*	*	*	*	*	*
All existing directors and executive officers as a group (seven individuals)	3,750,000	18.8%	3,750,000	7.7%	3,750,000	7.2%
All new directors and executive officers as a group (12 individuals)	*	*	37,258,065	69.1%	37,258,065	65.2%

* Less than one percent.

(1) Unless otherwise indicated, the business address of each of the individuals is 590 Madison Avenue, 21st Floor, New York, New York 10022.

(2) These shares are held by Tower Trust, a trust established for the benefit of Mr. Watson and his family.

(3) Ms. Kennedy s business address is c/o Robert F. Kennedy Center, 1367 Connecticut Avenue N.W., Suite 200, Washington, D.C. 20036.

(4) Mr. Hersov s business address is NetJets Europe, Ltd., Grundstrasse 12, 6343 Rotkreuz, Switzerland.

(5) Mr. Mathias business address is c/o The Carlyle Group, 1001 Pennsylvania Avenue, NW, Washington, DC 20004.

(6) Mr. Roberts business address is Roberts, Raheb & Gradler, 805 15th Street, NW, Suite 1101, Washington, DC 20005.

(7) The business address of T. Rowe Price Associates is 100 E. Pratt Street, Baltimore, Maryland 21202.

(8) Represents shares of common stock held by T. Rowe Price Associates, Inc. and T. Rowe Price New Horizons Fund, Inc. The foregoing information was derived from a Schedule 13G/A filed with the SEC on February 13, 2007.

(9) The business address of JLF Asset Management, L.L.C. is 2775 via de la Valle, Suite 204, Del Mar, CA 92014.

(10) Jeffrey L. Feinberg is the managing member of JLF Asset Management, L.L.C. The foregoing information was derived from a Schedule 13G filed with the SEC on January 29, 2007.

(11) The business address of Fir Tree, Inc. is 535 Fifth Avenue, 31st Floor, New York, New York 10017.

(12) Represents (i) 1,452,519 shares of common stock held by Sapling, LLC and (ii) 511,681 shares of common stock held by Fir Tree Recovery Master Fund, L.P. Fir Tree, Inc. is the investment manager of both entities. The foregoing information was derived from a Schedule 13G/A filed with the SEC on December 22, 2006.

(13) The business address of Prentice Capital Management, LP is 623 Fifth Avenue, 32nd Floor, New York, New York 10022.

(14) Represents shares held by investment funds for which Prentice Capital Management serves as investment manager. Michael Zimmerman is the managing member of Prentice Management GP, LLC, the general partner of Prentice Capital Management. The foregoing information was derived from a Schedule 13G filed with the SEC on May 17, 2006.

(15) The business address of Mr. Cohen is 72 Cummings Point Road, Stamford, Connecticut 06902.

(16) Represents (i) 1, 250,950 shares held by S.A.C. Capital Associates, Inc. (S.A.C), (ii) 250,600 shares held by CR Intrinsic Investors, LLC (CR) and (iii) 250,000 shares held by Sigma Capital Management, LLC (Sigma). Mr. Cohen controls CR and Sigma and S.A.C. Capital Advisors and S.A.C. Capital Management, which share all investment and voting power with respect to the securities held by S.A.C. The foregoing information was derived from a Schedule 13G/A filed with the SEC on February 14, 2007.

(17) The business address of Gilder, Gagnon, Howe & Co. LLC is 1775 Broadway, 26th Floor, New York, New York 10019.

Table of Contents

(18) Represents (i) 997,758 shares of common stock held in customer accounts over which partners and/or employees of Gilder, Gagnon, Howe & Co. LLC have discretionary authority to dispose of or direct the disposition of the shares, (ii) 55,543 shares of common stock held in accounts owned by the partners of Gilder, Gagnon, Howe & Co. LLC and their families, and (iii) 28,742 shares of common stock held in the account of the profit-sharing plan of Gilder, Gagnon, Howe & Co. LLC. The foregoing information was derived from a Schedule 13G filed with the SEC on March 12, 2007.
(19) The business address of FMR Corp. is 82 Devonshire Street, Boston, Massachusetts 02109.
(20) Represents shares of common stock under control of FMR Corp. and Edward C. Johnson 3d., its chairman. The foregoing information was derived from a Schedule 13G filed with the SEC on March 12, 2007.
(21) The business address of Morgan Stanley is 180 Madison Avenue, Suite 2305, New York, New York 10016.
(22) Represents 2,885,652 shares held by Morgan Stanley Investment Management Inc., a wholly-owned subsidiary of Morgan Stanley. The foregoing information was derived from a Schedule 13G filed with the SEC on April 9, 2007.
(23) The business address of Fred Alger Management, Inc. is 111 Fifth Avenue, New York, New York 10003.
(24) Represents 2,324,000 shares held by Fred Alger Management, Inc. (FAM) The Alger Family indirectly owns FAM. The foregoing information was derived from a Schedule 13G filed with the SEC on June 13, 2007.
(25) The business address of Scott A. Bommer is 767 Fifth Avenue, 21st Floor, New York, 10153.
(26) Represents (1) 803,177 shares held by SAB Capital Partners, L.P. (SAB), (ii) 18,566 shares held by SAB Capital Partners II, L.P. (SAB II) and, (iii) 343,267 shares held by SAB Overseas Master Fund, L.P. (Master Fund). Scott Bommer serves as managing member of each of SAB Capital Advisors, L.L.C., the general partner of SAB, SAB II and the Master Fund, and SAB Capital Management, L.L.C., the investment manager of SAB, SAB II and the Master Fund. The foregoing information was derived from a Schedule 13G filed with the SEC on May 14, 2007.
(27) The business address of Weiss Multi-Strategy Advisors LLC, George A. Weiss and Frederick E. Doucette III is One State Street, 20th Floor, Hartford CT 06103.
(28) Represents shares beneficially owned by Weiss Multi-Strategy Advisors LLC, George A. Weiss and Frederick E. Doucette III. The foregoing information was derived from a Schedule 13G filed with the SEC on October 25, 2007.
(29) The business address of each of these individuals is 747 Warehouse Street, Los Angeles, CA 90021.

Table of Contents

CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS

Endeavor Related Party Transactions

In July 2005, we issued 6,250,000 shares of our common stock to the Endeavor Inside Stockholders, comprised of the individuals set forth below for $25,000 in cash, at a purchase price of $0.004 share, as follows:

Stockholders	Number of Shares
Tower Trust	3,045,000
Jonathan J. Ledecky	3,045,000
Jay H. Nussbaum	40,000
Kerry Kennedy	40,000
Robert B. Hersov	40,000
Edward J. Mathias	40,000

On July 28, 2005, Messrs. Watson and Ledecky advanced an aggregate of $225,000 to us, on a non-interest bearing basis, for payment of offering expenses on our behalf. These amounts were repaid out of proceeds of our initial public offering.

On March 8, 2007, Endeavor borrowed funds from Messrs. Watson and Ledecky. Endeavor issued two promissory notes in the amount of $75,000 each. The principal balance of these notes shall be repayable on the earlier of the consummation of Endeavor s business combination with American Apparel or upon demand by Messrs. Watson and Ledecky. These promissory notes are noninterest bearing.

On April 30, 2007, Endeavor borrowed funds from Messrs. Watson and Ledecky. Endeavor issued two promissory notes in the amount of $87,500 each. The principal balance of these notes shall be repayable on the earlier of the consummation of Endeavor s business combination with American Apparel or upon demand by Messrs. Watson and Ledecky. These promissory notes are non-interest bearing.

On August 31, 2007, Endeavor borrowed funds from Messrs. Watson and Ledecky. Endeavor issued two promissory notes in the amount of $75,000 each. The principal balance of these notes shall be repayable on the earlier of the consummation of the Endeavor s business combination with American Apparel or upon demand by Messrs. Watson and Ledecky. These promissory notes are non-interest bearing.

On October 17, 2007, Endeavor borrowed funds from Messrs. Watson and Ledecky. Endeavor issued two promissory notes in the amount of $50,000 each for a total outstanding debt of $575,000 as of November 1, 2007. The principal balance of these notes shall be repayable on the earlier of the consummation of the Endeavor s business combination with American Apparel or upon demand by Messrs. Watson and Ledecky. These promissory notes are non-interest bearing.

In November 2005, each of Mr. Ledecky and Tower Trust transferred 20,000 shares of common stock to Richard Y. Roberts, a director of ours, for $0.004 per share (for an aggregate purchase price of $160). Additionally, in November 2005, Mr. Ledecky and Tower Trust contributed to us a total of 2,500,000 shares of common stock, effectively increasing the average purchase price to $0.0067 per share, and reducing the number of shares of our common stock held by the Endeavor Inside Stockholders to 3,750,000 shares.

We also entered into a registration rights agreement with the Endeavor Inside Stockholders pursuant to which the holders of the majority of their aggregate shares will be entitled to make up to two demands that we register these shares pursuant to an agreement to be signed prior to or on the date of this prospectus. The holders of the majority of these shares may elect to exercise these registration rights at any time commencing three months prior to the date on which these shares of common stock are released from escrow. In addition, these stockholders have certain piggy-back registration rights on registration statements filed subsequent to the date on which these shares of common stock are released from escrow. We will bear the expenses incurred in connection with the filing of any such registration statements.

Table of Contents

Each of the Endeavor Inside Stockholders also entered into a letter agreement with us and Ladenburg Thalmann pursuant to which, among other things:

- each agreed to vote all of the shares originally issued to him in accordance with the majority of the IPO Shares if we solicit approval of our stockholders for a business combination;

- if we fail to consummate a business combination by December 21, 2007, each agreed to take all reasonable actions within his power to cause us to liquidate as soon as reasonably practicable;

- each waived any and all rights he may have to receive any distribution of cash, property or other assets as a result of such liquidation with respect to his Founder Shares;

- each agreed to present to us for our consideration, prior to presentation to any other person or entity, any suitable opportunity to acquire an operating business, until the earlier of our consummation of a business combination, our liquidation or until such time as he ceases to be an officer or director of ours, subject to any pre-existing fiduciary obligations he might have. To that effect, Robert B. Hersov has pre-existing contractual and fiduciary obligations to Shine Media Acquisition Corp. Shine Media Acquisition Corp. is a blank check company formed to acquire a direct or indirect interest in an operating business in the media and advertising industry in the People s Republic of China. Mr. Hersov will honor his pre-existing contractual and fiduciary obligations to Shine Media Acquisition Corp. and present all suitable business opportunities that he may identify to it. Accordingly, he may not present opportunities to us that otherwise may be attractive to Shine Media Acquisition Corp. unless such entity has declined to accept such opportunities;

- each agreed that he and his affiliates will not be entitled to receive and will not accept any compensation for services rendered to us prior to the consummation of our business combination; and

- each agreed that he and his affiliates will not be entitled to receive or accept a finder s fee or any other compensation in the event he or his affiliates originate a business combination.

Pursuant to an escrow agreement between Endeavor, the Endeavor Inside Stockholders and Continental Stock Transfer & Trust Company (Continental), all of the shares listed above were placed in escrow, with Continental acting as escrow agent, pursuant to an escrow agreement, until the earliest of:

- December 21, 2008;

- Endeavor s liquidation;

- such date, following a business combination, that we consummated a liquidation, merger, stock exchange or other similar transaction which results in all of Endeavor s stockholders having the right to exchange their shares of common stock for cash, securities or other property subsequent to Endeavor s consummating a business combination with a target business;

- such date, following a business combination, as the last sales price of our common stock equals or exceeds $15.00 per share for any 20 trading days within any 30-trading day period.

During the escrow period, these shares cannot be sold, but the holders thereof will retain all other rights as stockholders, including, without limitation, the right to vote their shares of common stock and the right to receive cash dividends, if declared. If dividends are declared and payable in shares of common stock, such dividends will also be placed in escrow. If Endeavor is unable to effect a business combination and liquidate, none of Endeavor s Founders will receive any portion of the liquidation proceeds with respect to common stock owned by them prior to Endeavor s initial public offering.

From inception through January 1, 2007, Endeavor paid $7,500 per month to Ironbound Partners Fund, LLC, for general and administrative services. Ironbound is an affiliate of Jonathan Ledecky, Endeavor s president and secretary. This arrangement ceased as of January 1, 2007. From January 1, 2007 through April 2007, Endeavor paid a monthly rental of $3,000 for office space to an unaffiliated party. Endeavor was not

required to pay any rent for space during from May 2007 through October 2007. Commencing November 1, 2007 Endeavor is required to pay a monthly rental of $2,500 to another unaffiliated party for office space for the benefit of their consultants.

Other than the $7,500 per-month administrative fee and reimbursable out-of-pocket expenses previously paid to Ironbound, no compensation or fees of any kind, including finders and consulting fees, will be paid to any of our founders or to any of their respective affiliates for services rendered to us prior to or with respect to the business combination.

We will reimburse our officers and directors for any reasonable out-of-pocket business expenses incurred by them in connection with certain activities on our behalf such as identifying and investigating possible target businesses and business combinations.

From consummation of our IPO through the record date, Endeavor has borrowed an aggregate of $575,000 from Messrs. Watson and Ledecky. These loans are unsecured, non-interest bearing and will be repaid on the earlier of the consummation by Endeavor of a business combination or upon demand by Messrs. Ledecky and Watson; provided, however, that if a business combination is not consummated, Endeavor will be required to repay the loans only to the extent if has sufficient funds available to it outside of the trust account.

All ongoing and future transactions between Endeavor and any of its officers and directors or their respective affiliates, will be on terms believed by Endeavor to be no less favorable than are available from unaffiliated third parties and will require prior approval in each instance by a majority of the members of Endeavor s board who do not have an interest in the transaction.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities and Exchange Act of 1934, as amended, requires Endeavor directors, officers and persons owning more than 10% of Endeavor s common stock to file reports of ownership and changes of ownership with the SEC. Based on its review of the copies of such reports furnished to Endeavor, or representations from certain reporting persons that no other reports were required, Endeavor believes that all applicable filing requirements were complied with during the fiscal years ended December 31, 2005 and 2006 and as required through September 30, 2007.

Table of Contents

DESCRIPTION OF ENDEAVOR COMMON STOCK AND OTHER SECURITIES

General

The certificate of incorporation of Endeavor authorizes the issuance of 75,000,000 shares of common stock, par value $.0001, and 1,000,000 shares of preferred stock, par value $.0001. As of the record date, 19,910,745 shares of common stock were outstanding and no shares of preferred stock were outstanding.

Common Stock

The holders of common stock are entitled to one vote for each share held of record on all matters to be voted on by stockholders. In connection with the vote required for any business combination, all of the existing stockholders, including all officers and directors of Endeavor, have agreed to vote their respective shares of common stock owned by them immediately prior to the IPO in accordance with the vote of the public stockholders owning a majority of the shares of Endeavor s outstanding common stock. This voting arrangement does not apply to shares included in units purchased in the IPO or purchased following the IPO in the open market by any of Endeavor s stockholders, officers and directors. Endeavor s stockholders, officers and directors may vote their shares in any manner they determine, in their sole discretion, with respect to any other items that come before a vote of Endeavor s stockholders.

Endeavor will proceed with the acquisition only if the stockholders who own at least a majority of the shares of common stock sold in the IPO vote in favor of the acquisition and stockholders owning less than 20% of the shares sold in the IPO exercise conversion rights discussed below.

Endeavor s board of directors is divided into three classes, each of which will generally serve for a term of three years with only one class of directors being elected in each year. There is no cumulative voting with respect to the election of directors, with the result that the holders of more than 50% of the shares voted for the election of directors can elect all of the directors.

If Endeavor is required to liquidate, the holders of Endeavor common stock purchased in the IPO will be entitled to share ratably in the trust account, inclusive of any interest, and any net assets remaining available for distribution to them after payment of liabilities. Holders of common stock issued prior to Endeavor s IPO have agreed to waive their rights to share in any distribution with respect to common stock owned by them prior to the IPO if Endeavor is forced to liquidate.

Holders of Endeavor common stock do not have any conversion, preemptive or other subscription rights and there are no sinking fund or redemption provisions applicable to the common stock, except that the holders of Endeavor common stock acquired in the IPO have the right to have their shares of common stock converted to cash equal to their pro rata share of the trust account if they vote against the acquisition, properly demand conversion and the acquisition is approved and completed. Holders of common stock who convert their stock into their share of the trust account still have the right to exercise the warrants that they received as part of the units.

Preferred Stock

The certificate of incorporation of Endeavor authorizes the issuance of 1,000,000 shares of a blank check preferred stock with such designations, rights and preferences as may be determined from time to time by Endeavor s board of directors. Accordingly, Endeavor s board of directors is empowered, without stockholder approval, to issue preferred stock with dividend, liquidation, conversion, voting or other rights which could adversely affect the voting power or other rights of the holders of common stock, although Endeavor has entered into an underwriting agreement which prohibits Endeavor, prior to a business combination, from issuing preferred stock which participates in any manner in the proceeds of the trust account, or which votes as a class with the common stock on a business combination. Endeavor may issue some or all of the preferred stock to

effect a business combination. In addition, the preferred stock could be utilized as a method of discouraging, delaying or preventing a change in control of Endeavor. There are no shares of preferred stock outstanding and Endeavor does not currently intend to issue any preferred stock.

Warrants

Endeavor currently has outstanding 16,160,745 redeemable common stock purchase warrants. Each warrant entitles the registered holder to purchase one share of Endeavor s common stock at a price of $6.00 per share, subject to adjustment as discussed below, at any time commencing on the completion of the acquisition. The warrants expire on December 14, 2009 at 5:00 p.m., New York City time. Endeavor may call the warrants for redemption;

- in whole and not in part;
- at a price of $.01 per warrant at any time after the warrants become exercisable;
- upon not less than 30 days prior written notice of redemption to each warrant holder; and
- if, and only if, the reported last sale price of the common stock equals or exceeds $11.50 per share, for any 20 trading days within a 30 trading day period ending on the third business day prior to the notice of redemption to warrant holders.

Under the terms of the Acquisition Agreement, Endeavor has agreed that in connection with any redemption of the warrants, Endeavor would afford all of the holders thereof the right and opportunity to exercise their warrants on a cashless basis utilizing the value of such warrants based on the difference between the then current market price per share of Endeavor common stock and the pre-share exercise price of the warrants.

The exercise price and number of shares of common stock issuable on exercise of the warrants may be adjusted in certain circumstances including in the event of a stock dividend, or Endeavor s recapitalization, reorganization, merger or consolidation. However, the warrants will not be adjusted for issuances of common stock at a price below the exercise price.

The warrants may be exercised upon surrender of the warrant certificate on or prior to the expiration date at the offices of the warrant agent, with the exercise form on the reverse side of the warrant certificate completed and executed as indicated, accompanied by full payment of the exercise price, by certified check payable to Endeavor, for the number of warrants being exercised. The warrant holders do not have the rights or privileges of holders of common stock and any voting rights until they exercise their warrants and receive shares of common stock. After the issuance of shares of common stock upon exercise of the warrants, each holder will be entitled to one vote for each share held of record on all matters to be voted on by stockholders.

No warrants will be exercisable unless at the time of exercise a prospectus relating to common stock issuable upon exercise of the warrants is current and the common stock has been registered or qualified or deemed to be exempt under the securities laws of the state of residence of the holder of the warrants. Under the terms of a warrant agreement, Endeavor has agreed to maintain a current prospectus relating to common stock issuable upon exercise of the warrants until the expiration of the warrants. However, there is no assurance that Endeavor will be able to do so. The warrants may be deprived of any value and the market for the warrants may be limited if the prospectus relating to the common stock issuable upon the exercise of the warrants is not current or if the common stock is not qualified or exempt from qualification in the jurisdictions in which the holders of the warrants reside. If Endeavor is unable to deliver securities pursuant to the exercise of a warrant because a registration statement under the Securities Act of 1933, as amended, with respect to the Endeavor common stock is not effective, then in no event would Endeavor be obligated to pay cash or other consideration to the holders of warrants or otherwise net-cash settle any warrant exercise.

PRICE RANGE OF ENDEAVOR SECURITIES

Endeavor s units, common stock and warrants are traded on American Stock Exchange under the symbols EDA-U, EDA and EDA-WT, respectively. Each unit is comprised of one share of common stock and one warrant. The units commenced public trading on December 16, 2005, and the common stock and warrants commenced public trading on March 6, 2006. The following table sets forth the range of high and low closing bid prices for the units, common stock and warrants for the periods indicated.

	Units		Common Stock		Warrants	
	High	Low	High	Low	High	Low
2007:						
Fourth Quarter (through November 16, 2007)	20.06	16.93	13.40	11.84	6.75	5.24
Third Quarter	17.75	13.59	12.04	9.70	5.87	3.42
Second Quarter	19.45	14.40	12.90	9.92	6.50	3.95
First Quarter	17.50	11.91	12.06	9.18	5.60	3.05
2006:						
First Quarter	9.00	8.16	7.58	7.15	1.49	1.01
Second Quarter	9.00	7.92	7.55	7.25	1.55	0.96
Third Quarter	8.60	8.15	7.49	7.10	1.25	1.06
Fourth Quarter	12.00	8.10	9.31	7.28	3.05	1.02
2005:						
Fourth Quarter (commencing December 16, 2005)	8.10	7.98				

Holders of Endeavor common stock, warrants and units should obtain current market quotations for their securities. The market price of Endeavor common stock, warrants and units could vary at any time before the acquisition.

In connection with the acquisition, Endeavor and American Apparel will use their reasonable best efforts to maintain listing for trading on the American Stock Exchange of Endeavor s common stock, warrants and units. Endeavor believes it will meet the American Stock Exchange listing requirements upon consummation of the acquisition.

Holders

As of November 16, 2007, there were holders of record of Endeavor units, holders of record of Endeavor common stock and holders of record of Endeavor warrants. Endeavor believes that the beneficial holders of the units, common stock and warrants to be in excess of 1,000 persons each.

APPRAISAL RIGHTS

Endeavor stockholders do not have appraisal rights in connection the acquisition or the issuance of Endeavor common stock pursuant to the acquisition under the DGCL.

STOCKHOLDER PROPOSALS

The Endeavor 2008 annual meeting of stockholders will be held on or about September 24, 2008 unless the date is changed by the board of directors. If you are a stockholder and you want to include a proposal in the proxy statement for the year 2008 annual meeting, you need to provide it to us by no later than May 27, 2008. You should direct any proposals to our secretary at Endeavor s principal office which will be in Los Angeles, California. If you want to present a matter of business to be considered at the year 2008 annual meeting, under Endeavor s by-laws you must give timely notice of the matter, in writing, to our secretary. To be timely, the notice has to be given between 60 and 90 days. If Endeavor s is liquidated as a result of not consummating a business combination transaction before December 21, 2007, there will be no annual meeting in 2008.

Table of Contents

INDEPENDENT AUDITORS

The consolidated financial statements of AAI and its subsidiaries at December 31, 2006 and 2005 and for the years then ended included in this proxy statement, have been audited by Marcum & Kliegman LLP, an independent registered public accounting firm, as set forth in their report appearing elsewhere herein, and are included in reliance upon such report given on the authority of such firm as experts in accounting and auditing.

The combined financial statements of the CI companies at December 31, 2006 and 2005 and for the years then ended included in this proxy statement, have been audited by SNG Collins Barrow, S.E.N.C.R.L./LLP, an independent registered public accounting firm, as set forth in their report appearing elsewhere herein, and are included in reliance upon such report given on the authority of such firm as experts in accounting and auditing.

The financial statements of Endeavor at December 31, 2006, and 2005, the year ended December 31 2006 and the period from July 22, 2005 (inception) to December 31, 2005 included in this proxy statement have been audited by Marcum & Kliegman LLP, an independent registered public accounting firm, as set forth in their report appearing elsewhere herein, and are included in reliance upon such report given on the authority of such firm as experts in accounting and auditing.

Representatives of Marcum & Kliegman LLP will be present at the stockholder meeting or will be available by telephone with the opportunity to make statements and to respond to appropriate questions.

DELIVERY OF DOCUMENTS TO STOCKHOLDERS

Pursuant to the rules of the Securities and Exchange Commission, Endeavor and services that it employs to deliver communications to its stockholders are permitted to deliver to two or more stockholders sharing the same address a single copy of each of Endeavor s annual report to stockholders and Endeavor s proxy statement. Upon written or oral request, Endeavor will deliver a separate copy of the annual report and/or proxy statement to any stockholder at a shared address to which a single copy of each document was delivered and who wishes to receive separate copies of such documents in the future. Stockholders receiving multiple copies of such documents may likewise request that Endeavor deliver single copies of such documents in the future. Stockholders may notify Endeavor of their requests by calling or writing Endeavor at its principal executive offices at 590 Madison Avenue, New York, New York 10022.

WHERE YOU CAN FIND MORE INFORMATION

Endeavor files reports, proxy statements and other information with the SEC as required by the Securities Exchange Act of 1934, as amended. You may read and copy reports, proxy statements and other information filed by Endeavor with the SEC at the SEC public reference room located at 100 F Street, N.E., Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. You may also obtain copies of the materials described above at prescribed rates by writing to the SEC, Public Reference Section, 100 F Street, N.E., Washington, D.C. 20549. You may access information on Endeavor at the SEC web site containing reports, proxy statements and other information at: http://www.sec.gov.

Information and statements contained in this proxy statement or any annex to this proxy statement are qualified in all respects by reference to the copy of the relevant contract or other annex filed as an exhibit to this proxy statement.

All information contained in this document relating to Endeavor has been supplied by Endeavor, and all such information relating to American Apparel has been supplied by American Apparel. Information provided by one another does not constitute any representation, estimate or projection of the other.

Table of Contents

If you would like additional copies of this document or if you have questions about the acquisition, you should contact via phone or in writing:

Mr. Martin Dolfi

Endeavor Acquisition Corp.

590 Madison Avenue, 21st Floor

New York, New York 10022

212-683-5350 telephone

212-521-4389 telecopy

222

Table of Contents

INDEX TO FINANCIAL STATEMENTS

	Page
American Apparel and Subsidiaries	
Consolidated Interim Balance Sheets As of September 30, 2007 and 2006 (Unaudited)	FS-2
Consolidated Interim Statements of Operations For the Nine Months Ending September 30, 2007 and 2006 (Unaudited)	FS-3
Consolidated Interim Statement of Stockholders Equity and Comprehensive Income For the Nine Months Ended September 30, 2007 (Unaudited)	FS-4
Consolidated Interim Statements of Cash Flows For the Nine Months Ending September 30, 2007 and 2006 (Unaudited)	FS-5
Notes to Consolidated Interim Financial Statements (Unaudited)	FS-6
Report of Independent Registered Public Accounting Firm	FS-30
Consolidated Balance Sheets as of December 31, 2006 and 2005	FS-31
Consolidated Statements of Operations For the Years Ended December 31, 2006 and 2005	FS-33
Consolidated Statements of Stockholders Equity and Comprehensive Income (Loss) For the Years Ended December 31, 2006 and 2005	FS-34
Consolidated Statements of Cash Flows For the Years Ended December 31, 2006 and 2005	FS-35
Notes to Consolidated Financial Statements For the Years Ended December 31, 2006 and 2005	FS-37
Consolidated Balance Sheet as of December 31, 2004 (Unaudited)	FS-62
Consolidated Statement of Income Year Ended December 31, 2004 (Unaudited)	FS-63
Consolidated Statement of Stockholders Equity Year Ended December 31, 2004 (Unaudited)	FS-64
Consolidated Statement of Cash Flow Year Ended December 31, 2004 (Unaudited)	FS-65
Notes to Consolidated Financial Statements (Unaudited)	FS-66
American Apparel Canada Group Companies	
Combined Interim Balance Sheets As At September 30, 2007 and September 30, 2006 (in Canadian dollars) (Unaudited)	FS-79
Combined Interim Statements of Additional Paid in Capital and Retained Earnings for the Periods ended September 30, 2007 and September 30, 2006 (in Canadian Dollars) (Unaudited)	FS-80
Combined Interim Statements of Operations For The Periods Ended September 30, 2007 and September 30, 2006 (in Canadian Dollars) (unaudited)	FS-81
Combined Interim Statements of Cash Flows (Note 17) For The Periods Ended September 30, 2007 and September 30, 2006 (in Canadian Dollars) (unaudited)	FS-82
Notes To The Combined Interim Financial Statements As At September 30, 2007 and September 30, 2006 (in Canadian Dollars) (unaudited)	FS-83
Report of Independent Registered Public Accounting Firm	FS-99
Combined Balance Sheets As At December 31, 2006 (audited) 2005 (audited) and 2004 (unaudited) (in Canadian Dollars)	FS-100
Combined Statements of Additional Paid In Capital And Retained Earnings For The Years Ended December 31, 2006 (audited) 2005 (audited) and 2004 (unaudited) (in Canadian Dollars)	FS-101
Combined Statements of Operations For The Years Ended December 31, 2006 (audited), 2005 (audited) and 2004 (unaudited) (in Canadian Dollars)	FS-102
Combined Statements of Cash Flows For The Years Ended December 31, 2006 (audited, 2005 (audited) and 2004 (unaudited) (in Canadian dollars)	FS-103
Notes to Combined Financial Statements (in Canadian dollars)	FS-104
Endeavor Acquisition Corp.	
Condensed Balance Sheets	FS-121
Condensed Statements of Operations (unaudited) For the Nine Months Ended September 30, 2007 and 2006, and the Period July 22, 2005 (inception) to September 30, 2007	FS-122
Condensed Statement of Stockholders Equity (unaudited) For the Period July 22, 2005 (inception) to September 30, 2007	FS-123
Condensed Statements of Cash Flows (unaudited) For the Nine Months Ended September 30, 2007 and 2006 and For the Period July 22, 2005 (inception) to September 30, 2007	FS-124
Notes To Unaudited Condensed Financial Statements For The Nine Months Ended September 30, 2007 And 2006 And The Period July 22, 2005 (inception) To September 30, 2007	FS-125
Report of Independent Registered Public Accounting Firm	FS-132
Balance Sheet	FS-133
Statement of Operations	FS-134

Statement of Changes in Stockholders Equity From July 22, 2005 (Inception) to December 31, 2006	FS-135
Statement of Cash Flows	FS-136
Notes to Financial Statements	FS-137

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Balance Sheets

September 30, 2007 and 2006

(Unaudited)

(Dollars and Shares In Thousands)

	2007	2006
ASSETS		
CURRENT ASSETS		
Cash	$ 6,490	$ 4,371
Receivables		
Trade, net of allowances of $1,997 and $1,567 at September 30, 2007 and 2006, respectively	20,497	16,095
Due from Canadian Affiliate		314
Other	771	486
Prepaid expenses and other current assets	2,766	1,611
Inventories, net	91,324	76,079
Deferred tax asset	336	
Total Current Assets	122,184	98,956
PROPERTY AND EQUIPMENT, net	48,532	41,083
INTANGIBLE ASSETS, net	1,062	871
GOODWILL	950	950
OTHER ASSETS	10,228	6,446
TOTAL ASSETS	$ 182,956	$ 148,306
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES		
Cash overdraft	$ 4,858	$ 5,257
Current portion of bank debt	365	5,116
Notes payable to unrelated parties	5,639	4,106
Notes payable to related parties	4,380	4,258
Subordinated notes payable to related parties	360	360
Accounts payable	13,354	25,637
Accrued expenses	13,776	10,994
Due to Canadian Affiliate	660	
Income taxes payable	4,280	367
Current portion of capital lease obligations	3,091	2,735
Total Current Liabilities	50,763	58,830
LONG-TERM BANK DEBT, Net of current portion	102,106	52,077
SUBORDINATED NOTE PAYABLE TO UNRELATED PARTY		13,990
CAPITAL LEASE OBLIGATIONS, Net of current portion	3,681	3,695
DEFERRED RENT	7,677	6,307
TOTAL LIABILITIES	164,227	134,899
COMMITMENTS AND CONTINGENCIES		

STOCKHOLDERS EQUITY		
Common stock, no par value, 1,000 shares authorized, 100 shares issued and outstanding		
Additional paid-in capital	5,706	5,706
Due from stockholders	(767)	(199)
Accumulated other comprehensive income	504	171
Retained earnings	13,286	7,729
TOTAL STOCKHOLDERS EQUITY	18,729	13,407
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 182,956	$ 148,306

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statements of Operations

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

	2007	2006
NET SALES (including sales to the Canadian Affiliate of $9,217 and $9,724, for the nine months ending September 30, 2007 and 2006, respectively)	$ 254,837	$ 196,745
COST OF SALES (including cost of sales to the Canadian Affiliate of $8,941 and $9,433, for the nine months ending September 30, 2007 and 2006, respectively)	119,103	106,064
GROSS PROFIT	135,734	90,681
OPERATING EXPENSES (Reclassified-see Note 23)		
Selling	72,631	52,102
Warehouse and distribution	4,956	4,295
General and administrative (including related party rent expense of $477 and $ 0, for the nine months ended September 30 2007 and 2006, respectively)	30,683	25,991
TOTAL OPERATING EXPENSES	108,270	82,388
INCOME FROM OPERATIONS	27,464	8,293
INTEREST AND OTHER (INCOME) EXPENSE		
Interest expense (including related party interest expense of $658 and $154 for the nine months ended September 30 2007 and 2006, respectively)	12,255	7,869
Foreign currency gain	(20)	(436)
Other (income) expense	(1,077)	86
TOTAL INTEREST AND OTHER (INCOME) EXPENSE	11,158	7,519
INCOME BEFORE INCOME TAXES	16,306	774
INCOME TAX PROVISION	4,725	959
NET INCOME (LOSS)	$ 11,581	$ (185)

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statement of Stockholders Equity and Comprehensive Income

For the Nine Months Ended September 30, 2007

(Unaudited)

(In Thousands)

	Outstanding Shares	Amount	Additional Paid-in Capital	Due from Stockholders	Accumulated Other Comprehensive Income	Retained Earnings	Stockholders Equity	Comprehensive Income
BALANCE, January 1, 2007	100	$	$ 5,706	$ (553)	$ 322	$ 6,227	$ 11,702	
Advances to stockholders				(214)			(4,736)	
Distributions to stockholders				—		(4,522)		
Components of comprehensive income:								
Net income						11,581	11,581	$ 11,581
Foreign currency translation					182		182	182
								$ 11,763
BALANCE,								
September 30, 2007	100	$	$ 5,706	$ (767)	$ 504	$ 13,286	$ 18,729	

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers (including cash received from sales to Canadian Affiliate of $8,893 and $10,850, for the nine months ended September 30, 2007 and 2006, respectively)	$ 250,634	$ 193,406
Cash paid to suppliers, employees and others	(249,258)	(182,894)
Income taxes paid	(1,885)	(1,152)
Interest paid	(12,386)	(7,869)
Other	266	12
Net cash (used in) provided by operating activities	(12,629)	1,505
CASH FLOWS USED IN INVESTING ACTIVITIES		
Purchases of property and equipment	(10,892)	(13,085)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash overdraft from financial institution	1,897	1,524
Borrowings under revolving credit facility, net	1,542	6,029
Advances to stockholders	(214)	(41)
Distribution to stockholders	(4,522)	(633)
Advances from Canadian Affiliate, net	324	1,126
Deferred merger costs	(549)	
Deferred financing costs	(1,630)	
Borrowings of notes payable to related party	703	3,383
Borrowings under notes payable to unrelated parties	1,932	2,321
Repayment under notes payable to unrelated parties	(1,178)	(1,079)
(Repayments of) Borrowings under subordinated note payable to unrelated party	(14,201)	614
Borrowings under term loans and notes payable	51,346	7,716
Repayment of term loans and notes payable	(6,332)	(5,155)
Repayment of capital lease obligations	(2,518)	(2,373)
Net cash provided by financing activities	26,600	13,432
EFFECT OF FOREIGN EXCHANGE RATE ON CASH	197	137
NET CHANGE IN CASH	3,276	1,989
CASH, beginning of period	3,214	2,382
CASH, end of period	$ 6,490	$ 4,371
RECONCILIATION OF NET INCOME (LOSS) TO NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES		
Net income (loss)	$ 11,581	$ (185)
Depreciation and amortization	8,057	7,299
Foreign Currency transaction gain	(20)	(436)
Deferred rent	1,022	1,434
Bad debt expense (recovered)	(329)	667
Changes in cash due to changes in operating assets and liabilities		

Trade receivables	(3,183)	(4,745)
Other receivables	(502)	316
Inventories	(14,499)	(8,303)
Prepaid expenses and other current assets	(1,421)	78
Other assets	(2,505)	(3,157)
Accounts payable	(16,810)	7,297
Accrued expenses	3,140	1,336
Income taxes payable	2,840	(96)
Net cash (used-in) provided by operating activities	$ (12,629)	1,505
NON-CASH INVESTING AND FINANCING ACTIVITIES		
Property and equipment acquired under a capital lease	$ 3,226	$ 1,829

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

NOTE 1 Organization and Business

American Apparel, Inc. (AA), a California corporation is a vertically-integrated manufacturer, distributor and retailer of branded fashion basic apparel for men, women and children. AA sells its products through a wholesale distribution channel supplying t-shirts and other casual wear to distributors and screen printers, as well as direct to end users through retail stores located in the United States and internationally. In addition, AA operates an online retail e-commerce website. AA, collectively with its subsidiaries is referred to as the Company .

As of September 30, 2007 and 2006, the Company had 96 and 90 retail stores in the United States and 44 and 28 retail stores internationally, respectively.

The Company maintains its corporate offices, primary manufacturing and distribution facility, knitting and dye house in Los Angeles, California. The Company also maintains a portion of its yarn at outside knitting facilities and a portion of its greige goods at outside dye houses.

The wholly-owned operating subsidiaries of the Company are:

Sales

United States: American Apparel Retail, Inc. (AAR) operates retail stores. American Apparel Retail 1090 Third NYC, Inc., a wholly-owned subsidiary of AAR, operates a retail store in New York.

Mexico: American Apparel Mexico, S DE RL DE CU (AAM) operates retail stores. American Apparel Mexico Labor, LLC operates a payroll company used to provide services exclusively for AAM.

Continental Europe: American Apparel Deutschland GmbH operates retail stores and distributes American Apparel products.

United Kingdom: American Apparel (Carnaby) Limited operates retail stores. American Apparel (UK) Limited distributes American Apparel products.

Israel: American Apparel Retail (Israel), Ltd. operates a retail store.

Japan: American Apparel Japan Co., Ltd. operates retail stores and distributes American Apparel products.

Korea: American Apparel Korea Co., Ltd. operates retail stores, distributes, and franchises American Apparel products.

Manufacturing

KCL Knitting, LLC is engaged in textile manufacturing. The operating agreement under which KCL conducts its business provides that the term of their existence should continue until December 31, 2050.

American Apparel Dyeing and Finishing, Inc. operates a fabric dyeing and finishing plant.
In June 2007, the Company registered a wholly owned subsidiary in Australia called American Apparel Australia Pty Ltd. This subsidiary operates an online store in Australia which commenced operations in August 2007.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

NOTE 2 Summary of Significant Accounting Policies

Liquidity Matters

Over the past year, the Company s growth has been funded through a combination of borrowings from related and unrelated parties, bank debt, and lease financing. As of September 30, 2007 the Company had approximately $6,490 in unrestricted cash. During July 2007, the Company executed an agreement to obtain an additional $10 million in financing from its private investment firm. The Company also replaced its revolving credit facility of $62,500 (Note 9) with an increased revolving facility of $75,000 from a new bank. The Company believes that as a result of this it currently has sufficient cash and financing commitments to meet its funding requirements through at least September 30, 2008. The Company expects that it will need to obtain additional financing in order to accomplish its business plan over the next several years. There can be no assurance as to the availability or terms upon which such financing might be available. As of September 30, 2007, the Company failed to meet certain debt covenants relating to its financing agreements with its bank and private investment firm (Note 9). During November 2007, the Company obtained waivers from both the bank and its private investment firm for the violation of certain covenants. As a result of the waivers, the Company is currently in compliance with covenants set forth by the credit facility agreement and its term loan agreement and accordingly the loan balances as of September 30, 2007 are classified as long term obligations.

As discussed above, Management has taken several actions to improve the financial position of the Company. The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. The financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should the Company not continue as a going concern.

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of American Apparel, Inc. and its direct and indirect wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated upon consolidation.

The financial information in this quarterly report reflects, in the opinion of management, all adjustments of a normal recurring nature necessary to present fairly the results for the interim period. Quarterly operating results are not necessarily indicative of the results that may be expected for other interim periods or the year ending December 31, 2007. The interim financial statements for the periods ended September 30, 2007 and 2006 were not required to be reviewed and therefore were not reviewed by an independent registered public accounting firm using professional review standards and procedures.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The most significant estimates include; sales returns

FS-7

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

and other allowances, allowance for doubtful accounts, inventory valuation and obsolescence, valuation and recoverability of long-lived intangible assets including the values assigned to acquired intangible assets, goodwill, property and equipment, income taxes; and accruals for the outcome of current litigation.

On a continual basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews, and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates.

Revenue Recognition

The Company recognizes product sales revenue when title and risk of loss have transferred to the customer, there is persuasive evidence of an arrangement, shipment and passage of title has occurred, the sales price is fixed or determinable and collectibility is reasonably assured. Revenue from wholesale product sales and on-line product sales are recorded at the time the product is shipped to the customer. With respect to its own retail store operations, the Company recognizes revenue upon the sale of its products to retail customers. The Company s net sales represent gross sales invoiced to customers, less certain related charges for discounts, returns, and other promotional allowances. Allowances provided for these items are presented in the consolidated financial statements primarily as reductions to sales and cost of sales (see Sales Returns and Other Allowances discussed below for further information).

The Company recognizes the sales from gift cards, gift certificates and store credits as they are redeemed for merchandise. Prior to redemption, the Company maintains an unearned revenue liability for gift cards, gift certificates and store credits until the Company is released from such liability. The Company s gift cards, gift certificates and store credits do not have expiration dates. The unearned revenue for gift cards, gift certificates and store credits are recorded in accrued expenses in the amount of $809 and $597 at September 30, 2007 and 2006, respectively.

Sales Returns and Other Allowances

Allowances For Sales Returns The Company analyzes sales returns in accordance with Statement of Financial Accounting Standard (SFAS) No. 48 Revenue Recognition When Right of Return Exists (SFAS 48). The Company is able to make reasonable and reliable estimates of product returns for its wholesale, on-line product sales and retail store sales based on the Company s past history. The Company also monitors the buying patterns of the end-users of its products based on sales data received by its retail outlets. Estimates for sales returns are based on a variety of factors including actual returns based on expected return data communicated to it by customers. Accordingly, the Company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates.

As with any set of assumptions and estimates, there is a range of reasonably likely amounts that may be calculated for each allowance above. However, the Company believes that there would be no significant difference in the amounts reported using other reasonable assumptions than what was used to arrive at each allowance. The Company regularly reviews the factors that influence its estimates and, if necessary, makes adjustments when it believes that actual product returns, credits and other allowances may differ from established reserves. Actual experience associated with any of these items may be significantly different than the Company s estimates.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to credit risk consist primarily of cash (the amounts of which may, at times, exceed Federal Deposit Insurance Corporation limits on insurable amounts) and trade accounts receivable, relating substantially to the Company s US wholesale segment. The Company mitigates its risk by investing in or through major financial institutions. The Company has approximately $3,953 and $4,043 held in foreign banks at September 30, 2007 and 2006, respectively.

The Company performs on-going credit evaluations of its customers and adjusts credit limits based upon payment history and the customer s current credit worthiness, as determined by the review of their current credit information. Collections and payments from customers are continuously monitored. The Company maintains an allowance for doubtful accounts, which is based upon historical experience as well as specific customer collection issues that have been identified. While such bad debt expenses have historically been within expectations and allowances established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Cash

The Company s cash balances represent cash on deposit held at banks.

Accounts Receivable

Accounts receivable primarily consists of trade receivables, including amounts due from credit card companies, net of allowances. Amounts due from credit card, debit card and electronic benefit transfer transactions as of September 30, 2007 and 2006 were approximately $2,257 And $1,213, respectively.

Inventories

Inventories are stated at the lower of cost or market. Cost is primarily determined on the first-in, first-out (FIFO) method. The cost elements of inventories include materials, labor and overhead. For the nine months ending September 30, 2007 and 2006 no one supplier provided more than 10% of the Company s raw material purchases.

The Company identifies potentially excess and slow-moving inventories by evaluating turn rates, inventory levels and other factors. Excess quantities are identified through evaluation of inventory agings, review of inventory turns and historical sales experiences. The Company provides lower of cost or market reserves for such identified excess and slow-moving inventories. At September 30, 2007 and 2006 the Company had a reserve for slow-moving inventories of $4,284 and $1,961, respectively. The Company s reserve for slow-moving inventories increased $0 and $1.61 million during the nine months ended September 30, 2007 and 2006, respectively.

The Company establishes a reserve for inventory shrinkage for each of its retail locations. The reserve is based on the historical results of physical cycle counts.

Property and Equipment

Property and equipment are carried at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of the related assets. The costs of normal maintenance and repairs are charged to expense

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

in the year incurred. Expenditures which significantly improve or extend the life of an asset are capitalized and depreciated over the asset s remaining useful life. Amortization of leasehold improvements is computed using the straight-line method over the shorter of the estimated useful lives of the related assets or the lease term. Upon sale or disposition, the related cost and accumulated depreciation are removed from the accounts and the resulting gain or loss, if any, is reflected in operations.

Goodwill and Other Intangible Assets

Goodwill represents the excess of purchase price over the fair value of identifiable net assets of companies acquired. Goodwill and other intangible assets acquired in a business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142, Goodwill and Other Intangible Assets (SFAS 142). The SFAS 142 goodwill impairment model is a two-step process. The first step compares the fair value of a reporting unit that has goodwill assigned to its carrying value. The Company estimates the fair value of a reporting unit by using a discounted cash flow model. If the fair value of the reporting unit is determined to be less than its carrying value, a second step is performed to compute the amount of goodwill impairment, if any. Step two allocates the fair value of the reporting unit to the reporting unit s net assets other than goodwill. The excess of the fair value of the reporting unit over the amounts assigned to its net assets other than goodwill is considered the implied fair value of the reporting unit s goodwill. The implied fair value of the reporting unit s goodwill is then compared to the carrying value of its goodwill. Any shortfall represents the amount of goodwill impairment. The Company has not had any goodwill impairment.

Other definite lived intangibles are amortized on a straight-line basis over periods not exceeding 10 years.

Impairment of Long-Lived Assets

The Company follows the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 requires evaluation of the need for an impairment charge relating to long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The estimated future undiscounted cash flows associated with the asset would be compared to the asset s carrying amount to determine if a write down to a new depreciable basis is required. If required, an impairment charge is recorded based on an estimate of future discounted cash flows. The Company did not recognize any impairment charges for its long-lived assets during the nine months ended September 30, 2007 and 2006, respectively.

Foreign Currency

The financial statements of international subsidiaries are translated into U.S. Dollars using the exchange rate at each balance sheet date for assets and liabilities and an average exchange rate for each period for revenues, expenses, gains and losses. Foreign currency transaction gains and losses are charged or credited to operations as incurred. Where the local currency is the functional currency (which is determined based on management s judgment and involves consideration of all relevant economic facts and circumstances affecting the subsidiary) translation adjustments are recorded as a separate component of stockholders equity. For the nine months ended September 30, 2007 and 2006 the Company recognized foreign currency transaction gains of $20 and $436, respectively.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

Income Taxes

The stockholders of American Apparel, Inc. and its U.S. subsidiaries, American Apparel Retail, Inc., American Apparel Retail 1090 Third NYC, Inc., and American Apparel Dyeing and Finishing, Inc. elected subchapter S corporation status. Earnings and losses for Federal tax reporting purposes are included in the personal tax returns of the stockholders. Accordingly, the Company does not incur additional Federal income tax obligations, and the consolidated financial statements do not include a provision for Federal income taxes. American Apparel, Inc. expects to pay the necessary distributions to satisfy the stockholders estimated personal income tax aggregate personal liabilities based upon the Company s taxable income. As defined in the definitive Acquisition Agreement with Endeavor Acquisition Corp. (Endeavor) (Note 22), upon consummation of the merger, the stockholders will receive distributions to satisfy the stockholders estimated personal tax liabilities, as defined per the agreement. This distribution will be for shareholders taxable income attributable to the subchapter S corporation status and for the period commencing January 1, 2006 through the effective date of the Acquisition Agreement. The distribution amount will be less all previous distributions made by the Company. For periods before January 1, 2006, the Company expects to pay the estimated tax liabilities of the individual stockholders. As of December 31, 2006, the estimated tax liabilities of the individual stockholders, attributable to the taxable income of the Company approximated $6,200. Through September 30, 2007, payments of $3,050 were made against these liabilities. Subsequent to September 30, 2007 and through October 31, 2007, additional payments of $400 were made against these liabilities. Where applicable, state income taxes are provided by the Company at applicable statutory rates multiplied by pre-tax income. The Company files income tax returns in various states. Some of these states accept subchapter S corporation status, while in some states, the Company is taxed at C Corporation tax rates and in the remaining states, the Company is taxed at reduced rates applicable to S corporations.

American Apparel Deutschland GmbH, American Apparel (UK) Limited, American Apparel (Carnaby) Limited, American Apparel Mexico S DE RL DE CU, American Apparel Mexico Labor, LLC, American Apparel Japan Co., Ltd., American Apparel Korea Co., Ltd. and American Apparel Retail (Israel), Ltd. are foreign domiciled entities subject to foreign income taxes on earnings in their respective jurisdictions.

KCL Knitting, LLC (KCL) is a limited liability company, classified as a pass-through entity for federal income tax purposes, which provides for profits and losses to be reported by American Apparel, Inc.

American Apparel, Inc. has unrecognized built-in gains of approximately $26 million resulting from its S corporation election. If any of the assets creating the unrecognized built-in gains are sold in the ten-year period ending July 1, 2014, AA is liable for Federal income taxes on those gains. The gain is determined by using the tax basis of the assets compared with the fair value of those assets at the time of the S corporation election. No deferred income taxes have been provided as the built-in gain relates primarily to intangible assets that are not expected to be sold within the ten year holding period.

The foreign entities have elected to be consolidated with the US entities for federal tax purposes. As such, all of the operations are included in the determination of the taxable income of American Apparel, Inc. Foreign income taxes paid internationally may be treated as foreign tax credits at the stockholder level as American Apparel, Inc. is taxed as an S corporation for federal tax purposes.

The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Deferred tax liabilities and assets are

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

determined based on the difference between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The Company estimates the degree to which tax assets and credit carryforwards will result in a benefit based on expected profitability by tax jurisdiction. A valuation allowance for such tax assets and loss carryforwards is provided when it is determined that such assets will more likely than not go unused. If it becomes more likely than not that a tax asset will be used, the related valuation allowance on such assets would be reversed. Management makes judgments as to the interpretation of the tax laws that might be challenged upon an audit and cause changes to previous estimates of tax liability. In addition, the Company operates within multiple taxing jurisdictions and is subject to audit in these jurisdictions. In management s opinion, adequate provisions for income taxes have been made for all years. If actual taxable income by tax jurisdiction varies from estimates, additional allowances or reversals of reserves may be necessary.

Fair Value of Financial Instruments

The Company s financial instruments include cash, accounts receivable, accounts payable, revolving line of credit, and long-term debt. The Company estimates that carrying amounts of all financial instruments described above approximate fair value based upon current market conditions, maturity dates, and other factors.

Advertising, Promotion and Catalog

The Company expenses the production costs of advertising the first time the advertising takes place. The advertising expenses for the nine months ended September 30, 2007 and 2006 amounted to $8,177 and $4,686, respectively and were included in Selling expense in the Consolidated Statements of Operations. The Company has cooperative advertising arrangements with certain vendors in its US wholesale segment. For the nine months ended September 30, 2007 and 2006, cooperative advertising expenses were $364 and $301, respectively.

Shipping and Handling Costs

The Company incurs shipping and handling costs in its operations. These costs consist of freight expenses incurred for third-party shippers to transport products to wholesale customers. They are included in Cost of Sales in the Consolidated Statements of Income. Amounts billed to customers are included in Net Sales.

Deferred Rent, Rent Expense and Tenant Allowances

The Company occupies its retail stores and combined corporate office, manufacturing, and distribution center under operating leases generally with terms of one to ten years. Some leases contain renewal options for periods ranging from five to fifteen years under substantially the same terms and conditions as the original leases. Most of the store leases require payment of a specified minimum rent, a contingent rent based on a percentage of the store s net sales in excess of a specified threshold, plus defined escalating rent provisions. The Company straight-lines and recognizes its rent expense over the term of the lease (including probable lease renewals), plus the construction period prior to occupancy of the retail location, using a mid-month convention. Also included in rent expense are payments of real estate taxes, insurance and certain common area and maintenance costs in addition to the future minimum operating lease payments. Certain lease agreements provide for the Company to receive lease inducements or tenant allowances from landlords to assist in the financing of certain property. These inducements are recorded as a deferred credit and amortized as a reduction of rent expense over the term of the related lease.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

Start-up Costs

The Company expenses as incurred all retail store start-up and organization costs, including travel, training, recruiting, salaries and other operating costs.

Web Site Development Costs

The Company capitalizes applicable costs incurred during the application and infrastructure development stage and expenses incurred during the planning and operating stage. As of September 30, 2007 and 2006, the Company had capitalized website development costs of $280 and $28, respectively, which are included in Property and equipment in the accompanying Consolidated Balance Sheets.

Self-insurance accruals

The Company self-insures a significant portion of expected losses under the workers compensation program. Accrued liabilities are recorded based on the Company s estimates of the ultimate costs to settle incurred claims, both reported and unreported.

Comprehensive Income

In accordance with SFAS No. 130, Reporting Comprehensive Income, the Company is required to display comprehensive income and its components as part of its complete set of financial statements (Note 17). Comprehensive income represents the change in stockholders equity resulting from transactions other than stockholder investments and distributions. Included in accumulated other comprehensive income (loss) are changes in equity that are excluded from the Company s net income, specifically, unrealized gains and losses on foreign currency translation adjustments.

The Company does not record deferred income taxes related to accumulated other comprehensive income due to its subchapter S election in the United States and the foreign entities are taxed as disregarded entities.

Seasonality

The company experiences seasonality in its operations. Historically, sales during the second and third fiscal quarters have generally been the highest, with sales during the first fiscal quarter the lowest. This reflects the combined impact of the seasonality of the wholesale and retail segments. Generally, the company s retail segment has not experienced the same pronounced sales seasonality as other retailers.

Accounting Pronouncements-Newly Issued

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes-an Interpretation of FASB Statement No. 109 (the Interpretation). The Interpretation establishes for all entities a minimum threshold for financial statement recognition of the benefit of tax positions, and requires certain expanded disclosures. The Interpretation is effective for fiscal years beginning after December 15, 2006, and is to be applied to all open tax years as of the date of effectiveness. The Company adopted the interpretation as of January 1, 2007 and such adoption did not have a material effect on the Company s consolidated financial statements (Note 17).

FS-13

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Adoption is required for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption of SFAS No. 157 is encouraged. The Company is currently evaluating the expected effect of SFAS No. 157 on its consolidated financial statements and is currently not yet in a position to determine such effects.

In September 2006, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108 (SAB 108) which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. SAB 108 is effective for fiscal years ending on or after November 15, 2006. The adoption of SAB 108 did not have a material impact on the Company s consolidated financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption is required for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. The Company is currently evaluating the expected effect of SFAS No. 159 on its consolidated financial statements and is currently not yet in a position to determine such effects.

The FASB ratified the consensuses reached in Emerging Issues Task Force (EITF) Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation) (EITF 06-3). The EITF reached a consensus that the scope of the Issue includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, and may include, but is not limited to, sales, use, value added, and some excise taxes. The presentation of taxes within the scope of this Issue on either a gross or a net basis is an accounting policy decision that should be disclosed. Furthermore, for taxes reported on a gross basis, a company should disclose the aggregate amount of those taxes in interim and annual financial statements for each period for which an income statement is presented if that amount is significant. The disclosures required under this consensus should be applied retrospectively to interim and annual financial statements for all periods presented, if those amounts are significant. The Company adopted EITF 06-3 on January 1, 2007. The adoption of EITF 06-3 did not have a significant impact on its consolidated financial position or results of operations. The Company currently records its sales net of any value added or sales tax.

All other recently issued accounting pronouncements are not expected to have a material impact on the Company s consolidated financial statements.

NOTE 3 Variable Interest Entities

In January 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51 (FIN 46). In December 2003, the FASB modified FIN 46 to make certain

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

technical corrections and address certain implementation issues that had arisen. FIN 46R provides a new framework for identifying variable interest entities (VIEs) and determining when a company should include the assets, liabilities, non-controlling interests and results of activities of a VIE in its consolidated financial statements.

In general, a VIE is a corporation, partnership, limited liability corporation, trust or any other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principle activities without additional subordinated financial support, (2) has a group of equity owners that are unable to make significant decisions about its activities, or (3) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by its operations.

The Company identified an affiliate in Canada (Canadian Affiliate) that is determined to be a VIE under the provisions of FIN 46R. The Company determined it is not the primary beneficiary of the VIE and, as a result, has not consolidated the entity at September 30, 2007 or 2006.

The Canadian Affiliate, which is indirectly owned by one of the Company s 50% owners, has been in business since 1994. The Canadian Affiliate through its combined group of related companies operates 25 and 24 retail stores in Canada, that sell the Company s products at September 30, 2007 and 2006, respectively. The Canadian Affiliate s total assets at September 30, 2007 and 2006 were approximately $17,642 USD and $16,376 USD, respectively. The Canadian Affiliate s total equity was $2,772 USD and $1,571 USD at September 30, 2007 and 2006, respectively. The Company sells the Canadian Affiliate merchandise on credit, with payment due 60 days from delivery. As of September 30, 2007 and 2006 the Company had accounts receivable from the Canadian Affiliate of $ and $314, respectively, and accounts payable to the Canadian Affiliate of $660 and $, respectively.

NOTE 4 Inventories, net

The components of inventories at September 30 are as follows:

	2007	2006
Raw materials	$ 27,261	$ 24,374
Work in process	3,177	2,477
Finished goods	60,886	49,228
Total	$ 91,324	$ 76,079

FS-15

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

NOTE 5 Property and Equipment

The components of property and equipment at September 30 are as follows:

	2007	2006	Depreciation and Amortization Period (Years)
Machinery and equipment	$ 20,847	$ 17,591	5-7 years
Furniture and fixtures	10,262	7,756	5 years
Computers and software	9,342	7,435	3-5 years
Automobiles	383	145	3 years
Leasehold Improvements	33,676	26,313	Shorter of the life of lease or useful life
Construction in progress	2,199	234	
	76,709	59,474	
Accumulated depreciation and amortization	(28,177)	(18,391)	
Total	$ 48,532	$ 41,083	

For the nine months ended September 30, 2007 and 2006, depreciation and amortization expense relating to property and equipment (including capitalized leases) was $8,004 and $7,230, respectively. At September 30, 2007 and 2006, property and equipment includes $7,380 and $6,651 for assets held under capital leases, respectively. Accumulated depreciation for these capital leases at September 30, 2007 and 2006 was $3,844 and $2,332, respectively.

NOTE 6 Goodwill and Other Intangible Assets

Goodwill

Goodwill of $950 is related to the acquisition of American Apparel Dyeing & Finishing, Inc. on June 2, 2005, and was assigned to the U.S. wholesale segment. There were no changes in the carrying amount of goodwill by segment for the nine months ended September 30, 2007 and 2006.

Intangible Asset, net

The carrying amounts of intangible assets at September 30, are as follows:

	2007 Carrying Amount	2006 Carrying Amount	Amortization Period (Years)
Definite lived intangible assets:			
Key money store leases	$ 521	$ 737	Life of lease
Lease rights	841	203	Life of lease
	1,362	940	
Accumulated Amortization	(300)	(69)	
Total	$ 1,062	$ 871	

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

Key money is the amount of funds paid to a landlord or tenant to acquire the rights of tenancy under a commercial property lease for a certain property. Key money represents the right to lease with an automatic right of renewal. This right can be subsequently sold by the Company or can be recovered should the landlord refuse to allow the automatic right of renewal to be exercised. Key money is amortized over the respective lease terms.

Lease rights are costs incurred to acquire the right to lease a specific property. A majority of our lease rights are related to premiums paid to landlords. Lease rights are recorded at cost and are amortized over the estimated useful term of the respective leases. Property lease terms are generally for ten years.

Aggregate amortization expense of other definite lived intangible assets included in the Consolidated Statement of Operations under the caption General and administrative expenses for the nine months ended September 30, 2007 and 2006 was approximately $53 and $69, respectively.

As of September 30, 2007 estimated amortization expense for each of the five succeeding years is as follows:

	Amount
2008	$ 123
2009	123
2010	123
2011	123
2012	123

NOTE 7 Other Assets

The components of other assets at September 30 are as follows:

	2007	2006
Lease security deposits	$ 7,157	$ 5,648
Deferred financing costs	1,037	
Deferred potential merger costs	549	
Worker s Compensation deposit		728
Other	1,485	70
Total	$ 10,228	$ 6,446

FS-17

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

NOTE 8 Accrued Expenses

The components of accrued expenses at September 30 are as follows:

	2007	2006
Accrued compensation and related taxes	$ 3,499	$ 2,775
Worker s Compensation self-insurance reserves	4,511	2,041
Sales, value added tax, property taxes	1,280	855
Accrued interest		5
Gift certificates	809	597
Other	3,677	4,721
Total	$ 13,776	$ 10,994

NOTE 9 Long-term Bank Debt

Long-term bank debt at September 30 consists of the following:

	2007	2006
Credit Line Facility		
Revolving Credit Facility, maturing July 2012 all long term (a)	$ 50,110	$ 47,954
Term Loans and Notes Payable		
Term loan with bank, maturing September 2007 (b)		5,000
Term loan with bank, maturing March 2010 (b)		2,016
Term loan with bank, maturing October 2007 (c)	5	67
Term loan with bank, maturing December 2008 (c)	244	440
Term loan with private investment firm, maturing November 2008 (d)	51,000	
Various notes payable (e)	46	292
Leasehold improvement note, maturing March 2010 (f)	90	128
Leasehold improvement note, maturing December 2009 (f)	656	1,296
Term loan with financing company, maturing April 2010 (g)	320	
	52,361	9,239
Total Long-Term Bank Debt	102,471	57,193
Less current portion of bank debt	(365)	(5,116)

Long-Term Bank Debt, net of current portion	$ 102,106	$ 52,077

(a) At September 30, 2006, the revolving credit facility with a bank provided for borrowings up to $57,500. Borrowings under the facility were subject to certain advance provisions established by the bank and were collateralized by substantially all assets of the Company. Interest under the agreement was at LIBOR (5.32% plus 2.5% at September 30, 2006 or the bank s prime rate (8.25% at September 30, 2006) plus 2.25%, at the Company s option. The interest rate was 7.82% at September 30, 2006. The facility was to expire in January 2010. Stockholders of the Company personally guaranteed the borrowings. On January 18, 2007, the Company negotiated an increase in the size of its credit facility from $57,500 to $62,500. Among other requirements, this facility agreement included a subjective acceleration clause and required the Company to maintain a lock box.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

On July 2, 2007, the Company replaced its secured revolving credit facility of $62,500 with an increased revolving credit facility of $75,000 from a new bank. The Company did not incur any losses for early extinguishment of debt with this transaction. Prepayment fees of $313 were expensed in July 2007. Borrowings under the facility are subject to certain advance provisions established by the bank and are collateralized by all assets of the Company. Interest under the agreement is at LIBOR plus 2% or Prime rate, at the Company s option. The credit facility expires at the earlier of July 2, 2012 or thirty days prior to the maturity date of the loan agreement with the private investment firm (January 18, 2009) unless its refinanced on terms acceptable to the bank in December 2008. The credit facility agreement requires the Company to comply with certain covenants. The average borrowings during the nine months ended September 30, 2007 and 2006 were $50,241 and $46,263, respectively. As of September 30, 2007, the Company failed to meet its Indebtedness and Other Obligations and Transactions with affiliates debt covenants as defined in the agreement, relating to the credit facility agreement with its bank. During November 2007, the Company obtained from the bank a waiver for the violation of these covenants. As a result of the waiver, the Company is currently in compliance with covenants set forth by the credit facility agreement and accordingly the loan balance as of September 30, 2007 is classified as a long term obligation.

(b) At September 30, 2006, the Company had two term loans with a bank. The first loan was payable in monthly installments of $417, including interest at prime plus 1% through September 2007. The balance at September 30, 2006 was $5,000. The second loan was payable in monthly installments of $48, including interest at prime (8.25% at September 30, 2006) plus 1% through March 2010. The balance at September 30, 2006 was $2,016. Both of these loans were secured by various unsecured equipment. On January 18, 2007, the Company completed a $41,000 secured debt financing with a private investment firm (see (d) below). A portion of the financing proceeds was used to pay off both of these loans without any prepayment penalty. No charges for early extinguishment of debt were incurred associated with this transaction.

(c) At September 30, 2007 and 2006, the Company has two term loans with a financial institution. The first loan is payable in monthly installments of $5, including interest at prime (8.25% at September 30, 2007 and 2006) plus 1% through October 2007. The balances at September 30, 2007 and 2006 were $5 and $67, respectively. The second loan is payable in monthly installments of $22, including interest at prime plus 1% through December 2008. The balances at September 30, 2007 and 2006 were $244 and $440, respectively. Both of these loans are secured by related equipment.

(d) At September 30, 2007, the Company has a term loan agreement with a private investment firm with a balance of $51,000. On July 2, 2007, the Company increased this secured debt financing from $41,000 to $51,000. Indebtedness under the agreement bears interest at 16% per annum, payable monthly and matures on November 30, 2008. The agreement requires the Company to meet certain financial covenants. In the event the Company is in default under the agreement, the interest rate increases to 21% per annum and the private investment firm has the right to demand payment in full of all outstanding indebtedness. The agreement does not allow any prepayments prior to January 18, 2008 and subsequent to that date, any prepayment shall include a prepayment premium equal to 3% of the amount prepaid. As of September 30, 2007, the Company failed to meet its Indebtedness and Other Obligations and Transactions with affiliates debt covenants as defined in the agreement relating to the term loan agreement with the private investment firm. During November 2007, the company obtained from the private investment firm a waiver for the violation of these covenants. As a result of the waiver, the Company is currently in compliance with covenants set forth by the term loan agreement and accordingly the loan balance as of September 30, 2007 is classified as a long term obligation.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

(e) At September 30, 2007 and 2006, the Company had various promissory notes payable in monthly installments aggregating $18 and $51, respectively including interest ranging from 4.6% to 11.9% and maturing at various dates through August 2011. The notes are collateralized by equipment.

(f) At September 30, 2007 and 2006, the Company had two leasehold improvement term loans. The first loan is payable in monthly installments of $3 through March 2010, including interest at a rate of 8%. The balances at September 30, 2007 and 2006 were $90 and $128, respectively. The second loan is payable in monthly interest only payments at 9% through December 2009. The balances at September 30, 2007 and 2006 were $656 and $1,296, respectively.

(g) At September 30, 2007, the Company has a term loan with a financing company payable in monthly installments of $11 through April 2011, including interest at a rate of 9%. The balance at September 30, 2007 was $320.

Required principal payments of long-term debt are as follows:

Twelve Months Ending September 30,	
2008	$ 365
2009	51,210
2010	50,888
2011	8
	$ 102,471

NOTE 10 Notes Payable to Unrelated Parties

Unsecured notes payable to certain unrelated individuals are due upon demand with interest ranging from 10% to 24% per annum. The balances outstanding at September 30, 2007 and 2006 were $5,639 and $4,106, respectively. Notes are personally guaranteed by a stockholder.

NOTE 11 Notes Payable to Related Parties

Unsecured notes payable to certain individuals related to a stockholder are due upon demand with interest ranging from 12% to 18% per annum. The balances outstanding at September 30, 2007 and 2006 were $4,380 and $4,258, respectively.

NOTE 12 Subordinated Notes Payable to Unrelated Party

The Company had a financing agreement for borrowings of $12,500 with an unrelated third party, (the current second lien lender). Interest on the loan was at a rate of 17%. The Company paid monthly interest payments at a rate of 11% on the current outstanding principal balance. The remaining unpaid portion of all monthly interest was added to the principal balance. The balance outstanding at September 30, 2006 was $13,990, which included accrued interest aggregating $1,490. On January 18, 2007, the Company completed a $41,000 secured debt financing with a private investment firm (Note 9). A portion of the financing proceeds were used to pay off this loan with the unrelated third party plus the accrued interest without any prepayment penalty. No charges for early extinguishment of debt were incurred associated with this transaction.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

NOTE 13 Subordinated Notes Payable to Related Parties

The Company has unsecured notes payable with a related party (relative of a stockholder), which are due upon demand with interest at 18%. The balance outstanding at September 30, 2007 and 2006 was $180, respectively. The note was subordinated to the interest of the bank which held the Company s current revolving credit facility as well as the interest of the bank which provided the new secured revolving credit facility on July 2, 2007 (Note 9).

The Company has an unsecured note payable to a stockholder which is due on demand with interest at 12%. The balance outstanding at September 30, 2007 and 2006 was $180, respectively. The note is subordinated to the interest of the bank which provided the new secured revolving credit facility on July 2, 2007 (Note 9).

NOTE 14 Capital Lease Obligations

The Company leases certain equipment under capital lease arrangements expiring at various times through 2011. The assets and liabilities under capital leases are recorded at the lower of the present values of the minimum lease payments or the fair values of the assets. The interest rates pertaining to these capital leases range from 6.00% to 18.00% (average interest rate is 11.9%).

Minimum future payments under these capital leases at September 30 are:

	2007	2006
Total future minimum lease payments	$ 7,578	$ 7,504
Less: amounts representing interest	(806)	(1,074)
Net minimum lease payments	6,772	6,430
Current portion	(3,091)	(2,735)
Long-term portion	$ 3,681	$ 3,695

NOTE 15 Related Party Transactions

In December 2005, the Company entered into an operating lease, which commenced on November 15, 2006, for its knitting facility with a related company, which is partially owned by the stockholders of the Company. The monthly lease payments are $48 and the lease expires in November 2011, with a five year extension, at the option of the Company.

NOTE 16 Comprehensive Income

Total comprehensive income for the Company includes net income (loss) and the effects of foreign currency translation, which are charged or credited to the accumulated other comprehensive income account within stockholders equity. Total comprehensive income for the nine months ended September 30 is as follows:

	2007	2006
Net income (loss), as reported	$ 11,581	$ (185)
Changes in:		
Foreign currency translation adjustments	182	320
Total Comprehensive Income	$ 11,763	$ 135

FS-21

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

The change in the cumulative foreign currency translation adjustment primarily relates to the Company s investment in its foreign subsidiaries and fluctuations in exchange rates between their local functional currencies and the U.S. Dollar.

The Company does not record deferred income taxes relating to accumulated other comprehensive income due to their Subchapter S election in the U.S. and the foreign entities taxes as disregarded entities.

NOTE 17 Income Taxes

On January 1, 2007 the Company adopted the provisions of the Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB No. 109 (FIN No. 48). FIN No. 48 addresses the determination of how tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under Fin No. 48, the Company must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate resolution. The Company did not recognize any additional liabilities for uncertain tax positions as a result of the implementation of FIN No. 48. There were no unrecognized tax benefits as of the date of adoption or as of September 30, 2007.

The Company s uncertain tax positions are related to tax years that remain subject to examination by the relevant taxing authorities. The Company is currently open to audit under the statute of limitations by the Internal Revenue Service for the fiscal year ended June 30, 2004 and the calendar years ended December 31, 2004 through December 31, 2006. The Company has been contacted by the Internal Revenue Service to commence an audit of the 2005 calendar year tax return. The audit is currently in its initial stages. The Company and its subsidiaries state and foreign tax returns are also open to audit under similar statute of limitations for the same tax years. The Company does not expect its unrecognized tax benefit position to change during the next twelve months. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position.

The Company accrues interest on unrecognized tax benefits as a component of income tax expense. Penalties, if incurred, would be recognized as a component of income tax expense. The Company had no such accrued interest or penalties included in the accrued liabilities associated with unrecognized tax benefits as of the date of adoption or as of September 30, 2007. The Company does not expect its unrecognized tax benefit position to change during the next twelve months. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position.

Pursuant to Internal Revenue Code Sections 382 and 383, the annual use of the Company s general business credit carryforwards may be limited if there is greater than a 50% cumulative change in ownership.

The difference between the federal statutory rate of 34% and the effective tax rate of approximately 30% and 10% for the nine months ended September 30, 2007 and 2006, respectively, is due to applying the annual expected effective tax rate to the interim period. The difference between the statutory rate and the effective tax rate is due to the impact of the Company s S Corporation status for federal income tax purposes with no federal tax imposed, state income taxes, and foreign taxes.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

For the nine months ending September 30, income tax expense differs from the amount computed by applying the federal statutory tax rate of 34% to income before income taxes as shown below:

	2007	2006
Computed expected income tax expense	$ 5,361	$ 5,012
Reduced Federal tax rate for S Corporations	(5,361)	(5,012)
State income taxes, net of Federal income tax benefit	550	
California enterprise zone tax credits	(2,124)	(2,125)
Change in valuation allowance	2,124	2,125
Foreign taxes	4,175	959
Income Tax Expense	$ 4,725	$ 959

NOTE 18 Commitments and Contingencies

Operating Leases

The Company conducts retail operations under operating leases, which expire at various dates through 2020. Future minimum rental payments, including related party lease (Note 15) (excluding real estate tax and maintenance costs) for retail locations and other leases that have initial or noncancelable lease terms in excess of one year at September 30, 2007 are as follows:

	Amount
2008	$ 26,222
2009	23,045
2010	20,236
2011	18,717
2012	17,374
Thereafter	55,252
Total	$ 160,846

Operating lease rent expense (including real estate taxes and maintenance costs) and leases on a month to month basis were approximately $22,738 and $18,681 for the nine months ending September 30, 2007 and 2006, respectively. The Company did not incur any contingent rent during the same period. Rent expense is included in Cost of sales and General and administrative expenses in the accompanying Consolidated Statements of Operations.

Sales Tax

The Company has been contacted by the California State Board of Equalization in regard to scheduling a Sales and Use Tax audit for the period January 1, 2002 through December 31, 2004. No provision has been made for any future assessment, if any, which might be determined by the State Board of Equalization at the outcome of the audit.

California Franchise Tax Board

The Company has been contacted by the California Franchise Tax Board in regard to scheduling an audit related to California Enterprise Zone Tax Credits taken by the Company for the 2001 and 2002 income tax years.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

No provision has been made for any future assessment, if any, which might be determined by the California Franchise Tax Board at the outcome of the audit. However, the California Enterprise Zone Tax Credits have a full valuation allowance at September 30, 2007 and 2006 (Note 17).

Internal Revenue Service

The Company has been contacted by the Internal Revenue Service in regard to performing an audit for the income tax year 2005. The audit commenced in 2007. At this time no determination can be made as to the outcome of the audit and therefore no provision has been made for any additional future assessment, if any, which might be determined by the Internal Revenue Service as the outcome of the audit.

Advertising

At September 30, 2007, the Company had approximately $1,929 in open advertising commitments, which primarily relate to print advertisements in various newspapers and magazines during the remainder of 2007 and 2008.

NOTE 19 Workers Compensation Self-Insurance Reserves

Self Insurance Reserves

The Company uses a combination of third-party insurance and/or self-insurance for a number of risks including workers compensation and general liability claims. General liability costs relate primarily to litigation that arises from store operations. Self-insurance reserves include estimates of both claims filed carried at their expected ultimate settlement value and claims incurred but not yet reported. The Company s estimated claim amounts are discounted using a rate with a duration that approximates the duration of the Company s self-insurance reserve portfolio. The Company s liability reflected on the Consolidated Balance Sheet represents an estimate of the ultimate cost of claims incurred as of the balance sheet date. In estimating this liability, the Company utilizes loss development factors based on Company-specific data to project the future development of incurred losses. Loss estimates are adjusted based upon actual claim settlements and reported claims. These projections are subject to a high degree of variability based upon future inflation rates, litigation trends, legal interpretations, benefit level changes and claim settlement patterns. Although the Company does not expect the amounts ultimately paid to differ significantly from its estimates, self-insurance reserves could be affected if future claim experience differs significantly from the historical trends and the assumptions applied.

The workers compensation liability is based on estimate of losses for claims incurred, but not paid at year end. Funding is made directly to the providers and/or claimants by the insurance company. To guarantee performance under the workers compensation program, as of September 30, 2007 and 2006, the Company has issued standby letters of credit in the amount of $5,940 and $3,256, respectively, with two insurance companies being the beneficiaries, through a bank along with cash deposits of $0 and $728 as of September 30, 2007 and 2006, respectively. At September 30, 2007 and 2006, the Company recorded a reserve of $4,511 and $2,041, respectively for potential losses on existing claims as such amounts are believed to be probable and reasonably estimable.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

NOTE 20 Business Segment and Geographic Area Information

Segment Information

The Company s management reporting system evaluates performance based on a number of factors; however, the primary measures of performance are the net sales and income or loss from operations of each segment, as these are the key performance indicators reviewed by management. Operating income or loss for each segment does not include corporate general and administrative expenses, interest expense and other miscellaneous income/expense items. Corporate general and administrative expenses include, but are not limited to: human resources, legal, finance, IT and various other corporate level activity related expenses. Such unallocated expenses remain within corporate. The accounting policies of all operating segments are the same as those described in the summary of significant accounting policies in Note 2.

The Company reports the following segments: US Wholesale, US Retail and All Other. All of the Company s sales fall into one of these segments. The US Wholesale consists of sales of undecorated apparel products made to third party embellishers and other apparel manufacturers directly as well as through distributors including sales to its Canadian Affiliate that operates 25 retail stores plus wholesale operations. Internet sales are also recorded in the US wholesale segment. US Retail is comprised of 96 Company owned retail stores operating in the United States selling the Company s apparel products directly to consumers. The All Other segment comprises the international subsidiaries in Israel, continental Europe, the United Kingdom, Mexico, Japan and Korea, which operate 44 retail stores along with wholesale operations. None of these operations meet any of the quantitative thresholds for separate disclosure, as defined in SFAS No. 131, Disclosures About Segments of an Enterprise and Related Disclosures.

The following table represents key financial information of the Company s business segments:

	For the nine months ended September 30, 2007			
	US Wholesale	US Retail	All Other	Consolidated
Net sales to external customers	$ 115,683	$ 80,411	$ 58,743	$ 254,837
Income from operations	15,160	16,397	11,408	42,965
Depreciation and amortization	3,655	3,192	1,210	8,057
Capital Expenditures	1,196	5,267	4,429	10,892
Deferred rent expense	(112)	1,056	78	1,022

	For the nine months ended September 30, 2006			
	US Wholesale	US Retail	All Other	Consolidated
Net sales to external customers	$ 105,330	$ 58,008	$ 33,407	$ 196,745
Income from operations	11,236	8,439	3,202	22,877
Depreciation and amortization	3,704	2,891	704	7,299
Capital Expenditures	942	9,643	2,500	13,085
Deferred rent expense	(44)	1,516	(38)	1,434

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

Reconciliation to Income Before Income Taxes for the nine months ended September 30,

	2007	2006
Consolidated Income from operations of reportable segments	$ 42,965	$ 22,877
Corporate expenses	(15,501)	(14,584)
Interest expense	(12,255)	(7,869)
Other income (expense)	1,077	(86)
Foreign currency gain	20	436
Consolidated Income Before Income Taxes	$ 16,306	$ 774

	2007	2006
Net sales by location of customer		
United States	$ 186,877	$ 153,615
Germany	31,567	16,855
Korea	7,163	3,795
Canada	9,217	9,724
United Kingdom	11,224	6,702
Japan	7,147	4,579
Other foreign countries	1,642	1,475
Total Consolidated Net Sales	$ 254,837	$ 196,745

Long-lived assets Property and equipment, net, as of September 30,

	2007	2006
United States	$ 38,195	$ 35,782
Germany	6,284	2,438
Japan	1,592	1,272
Korea	538	450
United Kingdom	1,759	930
Other foreign countries	164	211
Consolidated Long-lived Assets	$ 48,532	$ 41,083
Identifiable assets by segment		
US wholesale	$ 112,122	$ 110,267

US retail	47,189	26,255
All other	23,645	11,784
Total	$ 182,956	$ 148,306

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

Foreign subsidiaries accounted for the following percentages of assets and total liabilities as of September 30,

	2007	2006
Total assets	13%	8%
Total liabilities	6%	6%

Product Revenue

For the nine months ended September 30,

	2007	2006
Net sales by class of customer:		
Wholesale	$ 128,874	$ 113,095
Retail	125,963	83,650
Total Consolidated Net Sales	$ 254,837	$ 196,745

NOTE 21 Litigation

The Company is subject to various claims and contingencies in the ordinary course of its business, including those related to litigation, business transactions, employee-related matters and taxes, among others. When the Company is aware of a claim or potential claim, it assesses the likelihood of any loss or exposure. If it is probable that a loss will result and the amount of the loss can be reasonably estimated, the Company will record a liability for the loss. The liability recorded includes probable and estimable legal costs associated with the claim or potential claim. If the loss is not probable or the amount of the loss cannot be reasonably estimated, the Company discloses the claim if the likelihood of a potential loss is reasonably possible and the amount involved could be material.

The Company is currently involved in matters with a few ex-employees who have either filed claims or state intentions to file various claims against the Company with the courts and regulatory agencies, which relate to alleged labor law violations, sexual harassment and other vague employment claims. One such claim against the Company was filed during 2005. During 2006, the Company was notified by two other ex-employees with respect to potential claims against the Company. One of these two ex-employees filed their claim against Company in 2007. Since these matters are currently in discovery or still in the early stages, no determination can be made at this time as to their final outcome, nor can the range of potential loss be estimated.

During 2006, a complaint was also filed against the Company by a customer who is claiming that the Company improperly recorded personal information at the point of sale at one of the Company s retail locations. The Company is in the process of settling this matter and does not expect the settlement to be material, however, no determination can be made at this time as to the final outcome of the settlement.

In the third quarter of 2007, the Company reached a confidential financial settlement regarding allegations of copyright infringement relating to past advertisements. This settlement has not had a material adverse effect on the Company s financial position, results of operations or liquidity. The Company is in the process of setting up mediation with another party who claims certain ownership rights over these same past

advertisements.

On or about September 4, 2007, Hanesbrands, Inc. and related entities (collectively, Hanes) filed a lawsuit in the United States District Court for the Middle District of North Carolina captioned *Hanesbrands, Inc. el al v. American Apparel, Inc. and American Apparel Retail, Inc.,* Case No. 1:07-cv-00662. In that lawsuit, Hanes

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars in Thousands)

contends that the Company used Hanes trademarks BARELY THERE and/or BARELYTHERE without Hanes authorization or approval and, by so doing, falsely represented the source, affiliation or sponsorship of American Apparel products. The Company is in the process of settling this matter with Hanes and does not expect the settlement to be material, however, no determination can be made at this time as to the final outcome of the settlement.

On or about October 3, 2007, Ms. Sonja Klimp filed a lawsuit in the United States District Court for the Central District of California captioned as *Sonja Klimp v. American Apparel, Inc. and American Apparel Retail, Inc.*, Case No. CV07-06448. Ms. Klimp is claiming that American Apparel, Inc. and American Apparel, Retail, Inc., knowingly and willfully violated the Fair Credit Reporting Act (15 U.S.C. §1681 et seq.) by printing more than the last five digits of a person s credit card or debit card numbers and/or printing the expiration date of the person s credit card on receipts provided to customers. The lawsuit is seeking an order certifying this case as a class action, as well as injunctive relief and unquantified statutory and monetary damages. American Apparel denies the allegations and intends to aggressively defend this matter. Since this matter is currently in discovery and still in the early stages, no determination can be made at this time as to its final outcome, nor can the range of potential loss be estimated.

The above mentioned complaints seek unspecified judgments and attorney s fees and costs. Although the outcome of such items cannot be determined with certainty, the Company is of the opinion that the final outcome of these matters are either without merit or will not have a material adverse impact on its consolidated financial position or results of operations. Management intends to defend itself vigorously against the allegations in these complaints.

NOTE 22 Proposed Merger

On December 18, 2006, the Company signed a definitive merger agreement with Endeavor, a blank check company publicly listed on the American Stock Exchange. Upon consummation of the merger, the Company would become a wholly-owned subsidiary of Endeavor. However, since one of the stockholders of the Company would own a majority of the outstanding common stock of Endeavor, the merger is expected to be accounted for as a reverse acquisition. For accounting purposes, the transaction would be accounted for as a recapitalization of the Company. As part of the merger, the Canadian Affiliate is also being acquired by Endeavor.

The merger is subject to customary closing conditions, and is expected to close in the second half of 2007. As part of the agreement, the Company is required to achieve certain financial targets set forth in the agreement. However, the Company is not in compliance with the financial targets. The Company and Endeavor can terminate the agreement at any time if mutually agreed. The agreement will terminate if a closing does not occur by December 15, 2007, and is subject to the approval of Endeavor s stockholders. There can be no assurances that the merger will be completed.

On November 6, 2007, the Company entered into an amended Acquisition Agreement (Amended Agreement) under which we increased the number of Transaction Shares that will be issued at the closing of the acquisition from 32,258,065 to 37,258,065 while at the same time increasing the level of the Company s net debt above which there would be a downward adjustment in the number of shares issued at the closing of the acquisition from $110 million to $150 million. The Amended Agreement also increased the size of the 2007 performance equity plan from 2,710,000 shares to 7,710,000 shares and provides that stock awards for an aggregate of 2,710,000 shares to 7,710,000 shares and provides that stock awards for an aggregate of 2,710,000 shares would be allocated and issued thereunder after consummation of the closing and upon filing of an effective registration statement.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Nine Months Ended September 30, 2007 and 2006

(Unaudited)

(Dollars In Thousands)

NOTE 23

The Company has reclassified its previously issued September 30, 2007 and 2006 consolidated financial statements for certain operating expenses. This reclassification predominantly related to certain store retail rents that were previously included in General and Administrative which have been reclassified to Selling. The reclassification had no effect on the consolidated balance sheets, the statements of stockholders equity or reported net income (loss) for any period.

The effect on the Company s previously issued 2006 and 2005 financial statements is summarized as follows:

Statement of Operations for the nine months September 30, 2007

	Previously Reported	Increase (Decrease)	As Reclassified
Selling	52,284	20,347	72,631
Warehouse and Distribution	4,074	882	4,956
General and Administrative	51,911	(21,228)	30,683

Statement of Operations for the nine months September 30, 2006

	Previously Reported	Increase (Decrease)	As Reclassified
Selling	35,564	16,538	52,102
Warehouse and Distribution	4,284	11	4,295
General and Administrative	42,540	(16,549)	25,991

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders

of American Apparel, Inc.

We have audited the accompanying consolidated balance sheets of American Apparel, Inc. and Subsidiaries (the Company) as of December 31, 2006 and 2005. and the related consolidated statements of operations, stockholders equity and comprehensive income (loss) and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, 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 consolidated financial position of American Apparel, Inc. and Subsidiaries, as of December 31. 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with United States generally accepted accounting principles.

As disclosed in Note 23 to the consolidated financial Statements, the Company has reclassified its statement of operations for the years ended December 31, 2006 and 2005 for certain operating expenses. The reclassification had no effect on the consolidated balance sheets, statements of stockholders equity or reported net (loss) income for any period.

/s/ Marcum & Kliegman LLP

New York, NY

August 10, 2007, except for Note 23, as

to which the date is November 15, 2007

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Balance Sheets

(Dollars and shares in thousands)

December 31, 2006 and 2005

	2006	2005
ASSETS		
CURRENT ASSETS		
Cash	$ 3,214	$ 2,382
Receivables		
Trade, net of allowances of $2,163 and $1,085 at December 31, 2006 and 2005, respectively	13,969	12,111
Due from Canadian Affiliate		1,440
Other	1,344	736
Prepaid expenses and other current assets	1,670	1,592
Inventories, net	76,470	67,534
Deferred tax asset	336	
Total Current Assets	97,003	85,795
PROPERTY AND EQUIPMENT, Net	42,469	33,475
INTANGIBLE ASSETS, Net	1,062	325
GOODWILL	950	950
OTHER ASSETS	6,673	3,681
TOTAL ASSETS	$ 148,157	$ 124,226

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Balance Sheets, Continued

(Dollars and shares in thousands)

December 31, 2006 and 2005

	2006	2005
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES		
Cash overdraft	$ 2,962	$ 3,686
Current portion of bank debt	3,201	5,612
Notes payable to unrelated parties	6,259	2,840
Notes payable to related parties	2,391	888
Subordinated notes payable to related parties	360	360
Accounts payable	30,136	18,261
Accrued expenses	9,935	10,032
Due to Canadian Affiliate	336	
Income taxes payable	1,303	416
Current portion of capital lease obligations	2,911	2,820
Total Current Liabilities	59,794	44,915
LONG-TERM BANK DEBT, Net of current portion	52,728	42,963
SUBORDINATED NOTE PAYABLE TO UNRELATED PARTY	14,201	13,376
CAPITAL LEASE OBLIGATIONS, Net of current portion	3,078	4,153
DEFERRED RENT	6,654	4,873
TOTAL LIABILITIES	136,455	110,280
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY		
Common stock, no par value, 1,000 shares authorized, 100 shares issued and outstanding	$	$
Additional paid-in capital	5,706	5,706
Due from stockholders	(553)	(158)
Accumulated other comprehensive income (loss)	322	(149)
Retained earnings	6,227	8,547
TOTAL STOCKHOLDERS EQUITY	11,702	13,946
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 148,157	$ 124,226

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

FS-32

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statements of Operations

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

	2006	2005
NET SALES (including sales to the Canadian Affiliate of $10,295 and $10,850 for the years ended December 31, 2006 and 2005, respectively)	$ 264,691	$ 188,106
COST OF SALES (including cost of sales for the Canadian Affiliate of $10,113 and $10,525 for the years ended December 31, 2006 and 2005, respectively)	138,385	101,048
GROSS PROFIT	126,306	87,058
OPERATING EXPENSES (Reclassified See Note 23)		
Selling	73,506	45,767
Warehouse and distribution	6,681	4,160
General and administrative (including related party rent expense of $380 and $ for the years ended December 31, 2006 and 2005, respectively)	36,819	26,896
TOTAL OPERATING EXPENSES	117,006	76,823
INCOME FROM OPERATIONS	9,300	10,235
INTEREST AND OTHER (INCOME) EXPENSE		
Interest expense (including related party interest expense of $206 and $105 for the years ended December 31, 2006 and 2005, respectively)	10,797	6,258
Foreign currency transaction (gain) loss	(601)	358
Other income	(607)	(356)
(LOSS) INCOME BEFORE INCOME TAXES	(289)	3,975
INCOME TAX PROVISION	1,335	392
NET (LOSS) INCOME	$ (1,624)	$ 3,583

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statements of Stockholders Equity and Comprehensive Income (Loss)

(Dollars and shares in thousands)

For the Years Ended December 31, 2006 and 2005

	Outstanding Shares	Amount	Additional Paid-In Capital	Due from Stockholders	Accumulated Other Comprehensive (Loss) Income	Retained Earnings	Stockholders Equity	Total Comprehensive Income (Loss)
BALANCE, January 1, 2005	100	$	$ 5,706	$ (1,197)	$	$ 7,954	$ 12,463	
Reclassification of prior year distributions to stockholders				1,197		(1,197)		
Distributions to stockholders						(1,793)	(1,793)	
Advances to stockholders				(158)			(158)	
Components of comprehensive income:								
Net Income						3,583	3,583	$ 3,583
Foreign currency translation					(149)		(149)	(149)
								$ 3,434
BALANCE, December 31, 2005	100		5,706	(158)	(149)	8,547	13,946	
Advances to stockholders				(395)			(395)	
Distributions to stockholders						(696)	(696)	
Components of comprehensive loss:								
Net (Loss)						(1,624)	(1,624)	$ (1,624)
Foreign currency translation					471		471	471
								$ (1,153)
BALANCE, December 31, 2006	100	$	$ 5,706	$ (553)	$ 322	$ 6,227	$ 11,702	

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers (including cash received from sales to Canadian Affiliate of $10,295 and $10,850 for the years ended December 31, 2006 and 2005, respectively)	$ 263,790	$ 186,446
Cash paid to suppliers, employees and others	(244,063)	(181,478)
Interest paid	(9,607)	(6,257)
Income taxes paid	(845)	(86)
Other	611	259
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	9,886	(1,116)
CASH FLOWS USED IN INVESTING ACTIVITIES		
Purchases of property and equipment	(15,232)	(14,635)
Purchase of net assets under business acquisition		(1,224)
NET CASH USED IN INVESTING ACTIVITIES	(15,232)	(15,859)
CASH FLOWS FROM FINANCING ACTIVITIES		
Change in matured fund from factor, net		362
Cash overdraft from financial institution	(722)	2,385
Borrowings under revolving credit facility, net	6,643	10,220
Distributions to stockholders	(696)	(1,793)
Advances to stockholders	(395)	(158)
Advances to Canadian Affiliate, net	(1,776)	130
Borrowings of notes payable to related party	1,826	148
Repayment of notes payable to related parties		(24)
Borrowings under notes payable to unrelated parties	4,406	1,343
Repayment under notes payable to unrelated parties	(1,089)	(577)
Borrowing under subordinated note payable to related party	180	
Borrowing under subordinated note payable to unrelated party		5,000
Borrowings under term loans and notes payable	7,479	5,703
Repayment of term loans and notes payable	(6,714)	(1,652)
Repayment of capital lease obligations	(3,141)	(3,659)
NET CASH PROVIDED BY FINANCING ACTIVITIES	6,001	17,428
EFFECT OF FOREIGN EXCHANGE RATE ON CHANGES IN CASH	177	(136)
NET CHANGE IN CASH	832	317
CASH Beginning	2,382	2,065
CASH Ending	$ 3,214	$ 2,382

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

	2006	2005
RECONCILIATION OF NET (LOSS) INCOME TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES		
Net (Loss) Income	$ (1,624)	$ 3,583
Depreciation and amortization	9,430	5,370
Impairment charge	221	605
Foreign currency transaction (gain) loss	(601)	358
Inventory reserve	3,484	600
Bad debt expense	1,121	586
Deferred tax benefit	(348)	
Deferred rent	1,771	3,510
Changes in operating assets and liabilities, net of acquisition:		
Trade receivables	(775)	(877)
Other receivables		(711)
Inventories	(12,010)	(20,824)
Prepaid expenses	(278)	(1,334)
Deposits and other assets	(4,596)	(2,110)
Accounts payable	11,866	2,372
Accrued expenses	1,387	7,447
Income taxes payable	838	309
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ 9,886	$ (1,116)
NON-CASH INVESTING AND FINANCING ACTIVITIES		
Property and equipment acquired under capital leases	$ 2,156	$ 6,446
Fair value of assets acquired for acquisitions accounted for under the purchase method of accounting	$	$ 655
Conversion of accrued interest to subordinated note payable to unrelated party	$	$ 798
Reclassification of due from stockholders to distributions	$	$ 1,197
Services provided to acquire assets accounted for under the purchase method of accounting	$	$ 576

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

NOTE 1 Organization and Business

American Apparel, Inc. (AA), a California corporation is a vertically-integrated manufacturer, distributor and retailer of branded fashion basic apparel for men, women and children. AA sells its products through a wholesale distribution channel supplying t-shirts and other casual wear to distributors and screen printers, as well as direct to end users through retail stores located in the United States and internationally and its e-commerce website. As of December 31, 2006 and 2005, the Company had 93 and 66 retail stores in the United States and 31 and 17 retail stores internationally, respectively.

In addition, AA operates an online retail e-commerce website. AA, collectively with its subsidiaries is referred to as the Company .

The Company maintains its corporate offices, primary manufacturing and distribution facility, knitting and dye house in Los Angeles, California. The Company also maintains a portion of its yarn at outside knitting facilities and a portion of its greige goods at outside dye houses.

The wholly-owned operating subsidiaries of the Company are:

Sales

United States: American Apparel Retail, Inc. (AAR) operates retail stores. American Apparel Retail 1090 Third NYC, Inc., a wholly-owned subsidiary of AAR, operates a retail store in New York.

Mexico: American Apparel Mexico, S DE RL DE CU (AAM) operates retail stores. American Apparel Mexico Labor, LLC operates a payroll company used to provide services exclusively for AAM.

Continental Europe: American Apparel Deutschland GmbH operates retail stores and distributes American Apparel products.

United Kingdom: American Apparel (Carnaby) Limited operates retail stores. American Apparel (UK) Limited distributes American Apparel products.

Israel: American Apparel Retail (Israel), Ltd. operates a retail store.

Japan: American Apparel Japan Co., Ltd. operates retail stores and distributes American Apparel products.

Korea: American Apparel Korea Co., Ltd. operates retail stores, distributes, and franchises American Apparel products.

Manufacturing

KCL Knitting, LLC is engaged in textile manufacturing. The operating agreement under which KCL conducts its business provides that the term of their existence should continue until December 31, 2050.

American Apparel Dyeing and Finishing, Inc. operates a fabric dyeing and finishing plant.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

NOTE 2 Summary of Significant Accounting Policies

Liquidity Matters

Over the past year, the Company s growth has been funded through a combination of borrowings from related and unrelated parties, bank debt, and lease financing. As of December 31, 2006, the Company had approximately $3,200 of unrestricted cash. As of December 31, 2006 and 2005, the Company failed to meet certain debt covenants relating to its financing agreements with its bank (Note 10) and the current second lien lender (Note 13). As a result of these covenant violations, the Company was in default of provisions stipulated in its financing agreements. As discussed in Note 22, the Company obtained $41 million of financing from a new second lien lender during January 2007. In addition, during July 2007 the Company executed an agreement with a private investment firm whereby the Company borrowed an additional $10,000 and it also replaced its revolving credit facility of $62,500 (Note 10) with an increased revolving facility of $75,000 from a new bank. In connection with these financings, the amounts due to the Company s current second lien lender and certain term loans were paid in full. The Company believes that, as a result of this, it currently has sufficient cash and financing commitments to meet its funding requirements through at least December 31, 2007. The Company expects that it will need to obtain additional financing in order to accomplish its business plan over the next several years. There can be no assurance as to the availability or terms upon which such financing might be available.

As discussed above, Management has taken several actions to improve the financial position of the Company. The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. The financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should the Company not be unable to continue as a going concern.

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of American Apparel, Inc. and its direct and indirect wholly-owned subsidiaries: All intercompany accounts and transactions have been eliminated upon consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The most significant estimates include; sales returns and other allowances, allowance for doubtful accounts, inventory valuation and obsolescence, valuation and recoverability of long-lived intangible assets including the values assigned to acquired intangible assets, goodwill, property and equipment, income taxes; and accruals for the outcome of current litigation.

On a continual basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews, and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

Revenue Recognition

The Company recognizes product sales revenue when title and risk of loss have transferred to the customer, there is persuasive evidence of an arrangement, shipment and passage of title has occurred, the sales price is fixed or determinable and collectibility is reasonably assured. Revenue from wholesale product sales and on-line product sales are recorded at the time the product is shipped to the customer. With respect to its own retail store operations, the Company recognizes revenue upon the sale of its products to retail customers. The Company s net sales represent gross sales invoiced to customers, less certain related charges for discounts, returns, and other promotional allowances. Allowances provided for these items are presented in the consolidated financial statements primarily as reductions to sales and cost of sales (see Sales Returns and Other Allowances discussed below for further information).

The Company recognizes the sales from gift cards, gift certificates and store credits as they are redeemed for merchandise. Prior to redemption, the Company maintains an unearned revenue liability for gift cards, gift certificates and store credits until the Company is released from such liability. The Company s gift cards, gift certificates and store credits do not have expiration dates, and the Company maintains full liability and does not recognize any revenue from gift cards, gift certificates and store credits until redemption takes place. The unearned revenue for gift cards, gift certificates and store credits are recorded in accrued expenses in the amount of $496 and $212 at December 31, 2006 and 2005, respectively.

Sales Returns and Other Allowances

Allowances For Sales Returns The Company analyzes sales returns in accordance with Statement of Financial Accounting Standard (SFAS) No. 48 Revenue Recognition When Right of Return Exists (SFAS 48). The Company is able to make reasonable and reliable estimates of product returns for its wholesale, on-line product sales and retail store sales based on the Company s past history. The Company also monitors the buying patterns of the end-users of its products based on sales data received by its retail outlets. Estimates for sales returns are based on a variety of factors including actual returns and based on expected return data communicated to it by customers. Accordingly, the Company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates.

As with any set of assumptions and estimates, there is a range of reasonably likely amounts that may be calculated for each allowance above. However, the Company believes that there would be no significant difference in the amounts reported using other reasonable assumptions than what was used to arrive at each allowance. The Company regularly reviews the factors that influence its estimates and, if necessary, makes adjustments when it believes that actual product returns, credits and other allowances may differ from established reserves. Actual experience associated with any of these items may be significantly different than the Company s estimates.

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to credit risk consist primarily of cash (the amounts of which may, at times, exceed Federal Deposit Insurance Corporation limits on insurable amounts) and trade accounts receivable, relating substantially to the Company s US wholesale segment. The Company mitigates its risk by investing in or through major financial institutions. The Company has approximately $2,100 and $1,470 held in foreign banks at December 31, 2006 and 2005, respectively.

The Company performs on-going credit evaluations of its customers and adjusts credit limits based upon payment history and the customer s current credit worthiness, as determined by the review of their current credit

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

information. Collections and payments from customers are continuously monitored. The Company maintains an allowance for doubtful accounts, which is based upon historical experience as well as specific customer collection issues that have been identified. While such bad debt expenses have historically been within expectations and allowances established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Cash

The Company s cash balances represent cash on deposit held at banks.

Accounts Receivable

Accounts receivable primarily consists of trade receivables, including amounts due from credit card companies, net of allowances. Amounts due from credit card, debit card and electronic benefits transfer transactions as of the balance sheet date of December 31, 2006 and 2005 were approximately $1,400 and $856, respectively, and represented amounts owed from third-party credit card issuers.

Inventories

Inventories are stated at the lower of cost or market. Cost is primarily determined on the first-in, first-out (FIFO) method. The cost elements of inventories include materials, labor and overhead. During 2006 and 2005 no one supplier provided more than 10% of the Company s raw material purchases.

The Company identifies potentially excess and slow-moving inventories by evaluating turn rates, inventory levels and other factors. Excess quantities are identified through evaluation of inventory aging, review of inventory turns and historical sales experiences. The Company provides lower of cost or market reserves for such identified excess and slow-moving inventories. During the years ended December 31, 2006 and 2005, the Company increased their reserve by $3,484 and $600, respectively, which resulted in a reserve for slow-moving inventories of $4,284 and $800 as of December 31, 2006 and 2005, respectively.

The Company establishes a reserve for inventory shrinkage for each of its retail locations. The reserve is based on the historical results of physical cycle counts.

Property and Equipment

Property and equipment are carried at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of the related assets. The costs of normal maintenance and repairs are charged to expense in the year incurred. Expenditures which significantly improve or extend the life of an asset are capitalized and depreciated over the asset s remaining useful life. Amortization of leasehold improvements is computed using the straight-line method over the shorter of the estimated useful lives of the related assets or the lease term. Upon sale or disposition, the related cost and accumulated depreciation are removed from the accounts and the resulting gain or loss, if any, is reflected in operations.

Goodwill and Other Intangible Assets

Goodwill represents the excess of purchase price over the fair value of identifiable net assets of companies acquired. Goodwill and other intangible assets acquired in a business combination and determined to have an

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142, Goodwill and Other Intangible Assets (SFAS 142). The SFAS 142 goodwill impairment model is a two-step process. The first step compares the fair value of a reporting unit that has goodwill assigned to its carrying value. The Company estimates the fair value of a reporting unit by using a discounted cash flow model. If the fair value of the reporting unit is determined to be less than its carrying value, a second step is performed to compute the amount of goodwill impairment, if any. Step two allocates the fair value of the reporting unit to the reporting unit s net assets other than goodwill. The excess of the fair value of the reporting unit over the amounts assigned to its net assets other than goodwill is considered the implied fair value of the reporting unit s goodwill. The implied fair value of the reporting unit s goodwill is then compared to the carrying value of its goodwill. Any shortfall represents the amount of goodwill impairment. The Company has not had any goodwill impairment.

Other definite lived intangibles are amortized on a straight-line basis over periods not exceeding 10 years.

Impairment of Long-Lived Assets

The Company follows the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 requires evaluation of the need for an impairment charge relating to long-lived assets, other than goodwill and indefinite-lived intangible assets, whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The estimated future undiscounted cash flows associated with the asset would be compared to the asset s carrying amount to determine if a write down to a new depreciable basis is required. If required, an impairment charge is recorded based on an estimate of future discounted cash flows. For the years ended December 31, 2006 and 2005, the Company recognized impairment charges of $221 and $605, respectively, on assets to be held and used. The impairment charges related primarily to leasehold improvements and furniture and fixtures for certain U.S. retail stores and were included in the Consolidated Statements of Operations under the caption General and administrative expenses.

Foreign Currency

The financial statements of international subsidiaries are translated into U.S. Dollars using the exchange rate at each balance sheet date for assets and liabilities and an average exchange rate for each period for revenues, expenses, gains and losses. Foreign currency transaction gains and losses are charged or credited to operations as incurred. Where the local currency is the functional currency (which is determined based on management s judgment and involves consideration of all relevant economic facts and circumstances affecting the subsidiary) translation adjustments are recorded as a separate component of stockholders equity. The Company recognized foreign currency transaction gains (losses) of $601 in 2006 and ($358) in 2005.

Income Taxes

The stockholders of American Apparel, Inc. and its U.S. subsidiaries, American Apparel Retail, Inc., American Apparel Retail 1090 Third NYC, Inc., and American Apparel Dyeing and Finishing, Inc. elected subchapter S corporation status. Earnings and losses for Federal tax reporting purposes are included in the personal tax returns of the stockholders. Accordingly, the Company does not incur additional Federal income tax obligations, and the consolidated financial statements do not include a provision for Federal income taxes. American Apparel, Inc. expects to pay the necessary distributions to satisfy the stockholders estimated personal

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

income tax aggregate personal liabilities based upon the Company s taxable income. As of December 31, 2006 and 2005, the estimated unpaid aggregate personal tax liabilities of the individual stockholders, attributable to the taxable income of the Company approximated $6,200 and $4,123 respectively. As defined in the definitive Acquisition Agreement with Endeavor Acquisition Corp. (Endeavor) (Note 22), upon consummation of the merger, the stockholders will receive distributions to satisfy the stockholders estimated personal tax liabilities, as defined per the agreement. This distribution will be for stockholders taxable income attributable to the subchapter S corporation status and for the period commencing January 1, 2006 through the effective date of the Acquisition Agreement. The distribution amount will be less all previous distributions made by the Company. For periods before January 1, 2006, the Company expects to pay the estimated tax liabilities of the individual stockholders subsequent to December 31, 2006 through July 31, 2007, payments of approximately $2,870 were made against these liabilities. Where applicable, state income taxes are provided by the Company at applicable statutory rates multiplied by pre-tax income. The Company files income tax returns in various states. Some of these states accept subchapter S corporation status, while in some states, the Company is taxed at C Corporation tax rates and in the remaining states, the Company is taxed at reduced rates applicable to S corporations.

American Apparel Deutschland GmbH, American Apparel (UK) Limited, American Apparel (Carnaby) Limited, American Apparel Mexico S DE RL DE CU, American Apparel Mexico Labor, LLC, American Apparel Japan, American Apparel Korea Co., Ltd. and American Apparel Retail (Israel), Ltd. are foreign domiciled entities subject to foreign income taxes on earnings in their respective jurisdictions.

KCL Knitting, LLC (KCL) is a limited liability company, classified as a pass-through entity for federal income tax purposes, which provides for profits and losses to be reported by American Apparel, Inc.

At December 31, 2006 and 2005, American Apparel, Inc. has unrecognized built-in gains of approximately $26 million resulting from its S corporation election. If any of the assets creating the unrecognized built-in gains are sold in the ten-year period ending July 1, 2014, AA is liable for Federal income taxes on those gains. The gain is determined by using the tax basis of the assets compared with the fair value of those assets at the time of the S corporation election. No deferred income taxes have been provided as the built-in gain relates primarily to intangible assets that are not expected to be sold within the ten year holding period.

The foreign entities have elected to be consolidated with the US entities for federal tax purposes. As such, all of the operations are included in the determination of the taxable income of American Apparel, Inc. Foreign income taxes paid internationally may be treated as foreign tax credits at the stockholder level as American Apparel, Inc. is taxed as an S corporation for federal tax purposes.

The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Deferred tax liabilities and assets are determined based on the difference between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The Company estimates the degree to which tax assets and credit carryforwards will result in a benefit based on expected profitability by tax jurisdiction. A valuation allowance for such tax assets and loss carryforwards is provided when it is determined that such assets will more likely than not go unused. If it becomes more likely than not that a tax asset will be used, the related valuation allowance on such assets would be reversed. Management makes judgments as to the interpretation of the tax laws that might be challenged upon an audit and cause changes to previous estimates of tax liability. In addition, the Company operates within multiple taxing jurisdictions and is subject to audit in these jurisdictions. In management s opinion, adequate provisions for income taxes have been

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

made for all years. If actual taxable income by tax jurisdiction varies from estimates, additional allowances or reversals of reserves may be necessary.

Fair Value of Financial Instruments

The Company s financial instruments include cash, accounts receivable, accounts payable, revolving line of credit, and long-term debt. The Company estimates that carrying amounts of all financial instruments described above approximate fair value based upon current market conditions, maturity dates, and other factors.

Advertising, Promotion and Catalog

The Company expenses the production costs of advertising the first time the advertising takes place. The advertising expenses for the years ended December 31, 2006 and 2005 amounted to $7,138 and $5,732, respectively, and were included in Selling expense in the Consolidated Statements of Operations. The Company has cooperative advertising arrangements with certain vendors in its US wholesale segment. Cooperative advertising expenses were $376 and $348 for the years ended December 31, 2006 and 2005, respectively.

Shipping and Handling Costs

The Company incurs shipping and handling costs in its operations. These costs consist of freight expenses incurred for third-party shippers to transport products to wholesale customers. They are included in Cost of Sales in the Consolidated Statements of Income and amounted to $6,471 and $4,461 for the years ended December 31, 2006 and 2005, respectively. Amounts billed to customers of $4,775 and $3,574 for the years ended December 31, 2006 and 2005, respectively are included in Net Sales.

Deferred Rent, Rent Expense and Tenant Allowances

The Company occupies its retail stores and combined corporate office, manufacturing, and distribution center under operating leases generally with terms of one to ten years. Some leases contain renewal options for periods ranging from five to fifteen years under substantially the same terms and conditions as the original leases. Most of the store leases require payment of a specified minimum rent, a contingent rent based on a percentage of the store s net sales in excess of a specified threshold, plus defined escalating rent provisions. The Company straight-lines and recognizes its rent expense over the term of the lease (including probable lease renewals), plus the construction period prior to occupancy of the retail location, using a mid-month convention. Also included in rent expense are payments of real estate taxes, insurance and certain common area and maintenance costs in addition to the future minimum operating lease payments. Certain lease agreements provide for the Company to receive lease inducements or tenant allowances from landlords to assist in the financing of certain property. These inducements are recorded as a deferred credit and amortized as a reduction of rent expense over the term of the related lease.

Start-up Costs

The Company expenses as incurred all retail store start-up and organization costs, including travel, training, recruiting, salaries and other operating costs.

Web Site Development Costs

The Company capitalizes applicable costs incurred during the application and infrastructure development stage and expenses incurred during the planning and operating stage. As of December 31, 2006 and 2005, the

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

Company capitalized website development costs approximating $273 and $0, which is included in Property and equipment in the accompanying Consolidated Balance Sheets.

Self-insurance accruals

The Company self-insures a significant portion of expected losses under its workers compensation program. Accrued liabilities are recorded based on the Company s estimates of the ultimate costs to settle incurred claims, both reported and unreported.

Comprehensive (Loss) Income

In accordance with SFAS No. 130, Reporting Comprehensive Income , the Company is required to display comprehensive income and its components as part of its complete set of financial statements. Comprehensive income represents the change in stockholders equity resulting from transactions other than stockholder investments and distributions. Included in accumulated other comprehensive income (loss) are changes in equity that are excluded from the Company s net (loss) income, specifically, unrealized gains and losses on foreign currency translation adjustments.

The Company does not record deferred income taxes relating to accumulated other comprehensive income due to its Subchapter S election in the U.S. and the foreign entities are taxed as disregarded entities.

Seasonality

The company experiences seasonality in its operations. Historically, sales during the second and third fiscal quarters have generally been the highest, with sales during the first fiscal quarter the lowest. This reflects the combined impact of the seasonality of the wholesale and retail segments. Generally, the Company s retail segment has not experienced the same pronounced sales seasonality as other retailers.

Accounting Pronouncements-Newly Issued

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB 43, Chapter 4. SFAS No. 151 clarifies that abnormal amounts of idle facility expenses, freight, handling costs and spoilage should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The provisions of SFAS No. 151 must be applied prospectively to the Company s inventory costs incurred after January 1, 2006. The adoption of SFAS No. 151 did not have a material impact on the Company s consolidated financial position or results of operations.

In May 2005, SFAS No. 154, Accounting Changes and Error Corrections replacement of APB Opinion No. 20 and FASB Statement No. 3, was issued. SFAS No. 154 changes the accounting for and reporting of a change in accounting principle by requiring retrospective application to prior periods financial statements of changes in accounting principle unless impracticable. SFAS No. 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 did not have a material impact on the Company s consolidated results of operations, financial position or cash flows.

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes-an Interpretation of FASB Statement No. 109 (the Interpretation). The Interpretation establishes for all entities a minimum threshold for financial statement recognition of the benefit of tax positions, and requires certain expanded disclosures. The Interpretation is

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

effective for fiscal years beginning after December 15, 2006, and is to be applied to all open tax years as of the date of effectiveness. The Company adopted the Interpretation as of January 1, 2007, and such adoption did not have a material impact on the Company s consolidated results of operations, financial position or cash flows.

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements , which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Adoption is required for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption of SFAS No. 157 is encouraged. The Company is currently evaluating the expected effect of SFAS No. 157 on its consolidated financial statements and is currently not yet in a position to determine such effects.

In September 2006, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108 (SAB 108) which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. SAB 108 is effective for fiscal years ending on or after November 15, 2006. The adoption of SAB 108 did not have a material impact on the Company s consolidated financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No. 115 (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption is required for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. The Company is currently evaluating the expected effect of SFAS No. 159 on its consolidated financial statements and is currently not yet in a position to determine such effects.

The FASB ratified the consensuses reached in Emerging Issues Task Force (EITF) Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation) (EITF 06-3). The EITF reached a consensus that the scope of the Issue includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, and may include, but is not limited to, sales, use, value added, and some excise taxes. The presentation of taxes within the scope of this Issue on either a gross or a net basis is an accounting policy decision that should be disclosed. Furthermore, for taxes reported on a gross basis, a company should disclose the aggregate amount of those taxes in interim and annual financial statements for each period for which an income statement is presented if that amount is significant. The disclosures required under this consensus should be applied retrospectively to interim and annual financial statements for all periods presented, if those amounts are significant. The Company adopted EITF 06-3 on January 1, 2007. The adoption of EITF 06-3 did not have a significant impact on its consolidated financial position or results of operations. The Company currently records its sales net of any value added or sales tax.

All other recently issued accounting pronouncements are not expected to have a material impact on the Company s consolidated financial statements.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

NOTE 3 Variable Interest Entities

In January 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51 (FIN 46). In December 2003, the FASB modified FIN 46 to make certain technical corrections and address certain implementation issues that had arisen. FIN 46R provides a new framework for identifying variable interest entities (VIEs) and determining when a company should include the assets, liabilities, non-controlling interests and results of activities of a VIE in its consolidated financial statements.

In general, a VIE is a corporation, partnership, limited liability corporation, trust or any other legal structure used to conduct activities or hold assets that either (1) has an insufficient amount of equity to carry out its principle activities without additional subordinated financial support, (2) has a group of equity owners that are unable to make significant decisions about its activities, or (3) has a group of equity owners that do not have the obligation to absorb losses or the right to receive returns generated by its operations.

The Company identified an affiliate in Canada (Canadian Affiliate) that is determined to be a VIE under the provisions of FIN 46R. The Company determined it is not the primary beneficiary of the VIE and, as a result, has not consolidated the entity at December 31 2006 or 2005.

The Canadian Affiliate, which is indirectly owned by one of the Company s 50% owners, has been in business since 1994. The Canadian Affiliate through its combined group of related companies operated 25 and 20 retail stores in Canada, that sell the Company s products, at December 31, 2006 and 2005, respectively. The Canadian Affiliate s total assets at December 31, 2006 and 2005 were approximately $15,534 and $14,834, respectively. The Canadian Affiliate s total equity was $1,462 and $1,259 at December 31, 2006 and 2005, respectively. The Company sells the Canadian Affiliate merchandise on credit, with payment due 60 days from delivery. As of December 31, 2006 and 2005 the Company had accounts receivable from the Canadian Affiliate of $0 and $1,440, respectively and accounts payable to the Canadian Affiliate of $336 and $0, respectively.

NOTE 4 Business Acquisitions

American Apparel Dyeing and Finishing, Inc., a wholly owned subsidiary of American Apparel, Inc. entered into an agreement on June 2, 2005 with E & J Textile Group to purchase all of the assets of its dye and fabric processing and finishing plant. The Company purchased E&J Textile Group so that it could dye its own fabric for use in the production of its apparel products. The assets purchased included all of the facility s tangible personal property. In addition, American Apparel Dyeing and Finishing, Inc. purchased the lease agreement for the premises and equipment leases. The Company accounted for this acquisition under the purchase method of accounting in accordance with SFAS No 141, Business Combinations . Under the purchase method the total purchase price has been allocated to the tangible and intangible assets acquired and liabilities assumed based upon their estimated fair values and the excess was allocated to goodwill.

The purchase price of the dye house facility amounted to $1,800. A payment was made at closing in the amount of approximately $1,224. Of this payment, approximately $900 was financed by a third party financial institution. The remaining balance of approximately $576 was paid off by future services rendered to the seller all of which were rendered and paid during the remainder of the year ended December 31, 2005. In addition to the purchase price, costs in the amount of approximately $371 were incurred and expensed during the year ended December 31, 2005. Prior to the acquisition, American Apparel Dyeing and Finishing, Inc. did not commence operations. The $900 financed by a third party financial institution was paid in full during the remainder of the year ended December 31, 2005.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

The following table summarizes the estimated fair values of assets purchased at the date of acquisition as of June 2, 2005:

Goodwill	$ 950
Property and equipment	600
Leasehold improvements	250
Total assets acquired	$ 1,800

On September 16, 2005, American Apparel Retail, Inc., acquired the net assets of an unrelated third party Company, distributor and franchiser of American Apparel products in order to own all of its retail stores under one parent company. The acquired Company, American Apparel Korea, Co. Ltd.,. became a wholly-owned subsidiary of American Apparel Retail, Inc. The purchase price of the Company amounted to approximately $655, payable by a promissory note at an interest rate of 9% per annum through September 2006. These consolidated financial statements include the results of operations of American Apparel Korea, Co. Ltd. since completion of this purchase transaction.

The following table summarizes the estimated fair values of assets acquired at the date of acquisition as of September 16, 2005:

Prepaid expenses	$ 53
Property and equipment	65
Deposits	69
Inventory	468
Total assets acquired	$ 655

In addition to these acquired net assets, the purchase price included 10 franchising contracts with retail stores throughout Korea. These franchising agreements are exclusively for the right to sell American Apparel Korea, Co. Ltd. products. Franchising agreements are all for the term of one year with an option to renew.

Pro-forma financial information is not provided for these acquisitions as their impact was not material individually or in the aggregate to the Company s consolidated financial statements.

NOTE 5 Inventories, net

The components of inventories at December 31 are as follows:

	2006	2005
Raw materials	$ 21,991	$ 25,006
Work in process	1,532	1,906
Finished goods	52,947	40,622

Total	$ 76,470	$ 67,534

FS-47

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

NOTE 6 Property and Equipment

The components of property and equipment at December 31 are as follows:

	2006	2005	Depreciation and Amortization Period (Years)
Machinery and equipment	$ 18,268	$ 15,626	5-7 years
Furniture and fixtures	8,292	6,019	5 years
Computers and software	8,134	6,417	3-5 years
Automobiles	319	80	3 years
Leasehold Improvements	27,298	16,425	Shorter of the life of lease or useful life
Construction in progress	334		
	62,645	44,567	
Accumulated depreciation and amortization	(20,176)	(11,092)	
Total	$ 42,469	$ 33,475	

For the years ended December 31, 2006 and 2005, depreciation and amortization expense relating to property and equipment (including capitalized leases) was $9,355 and $5,366, respectively. At December 31, 2006 and 2005, property and equipment includes $12,941 and $10,253 for assets held under capital leases, respectively. Accumulated depreciation and amortization for these capital leases at December 31, 2006 and 2005 was $6,019 and $3,000, respectively.

NOTE 7 Goodwill and Other Intangible Assets

Goodwill

Goodwill of $950 related to the acquisition of American Apparel Dyeing & Finishing, Inc. on June 2, 2005, (Note 5) and was assigned to the U.S. wholesale segment. There were no changes in the carrying amount of goodwill by segment for the year ended December 31, 2006.

Intangible Asset, net

The carrying amounts of intangible assets at December 31, are as follows:

	2006 Carrying Amount	2005 Carrying Amount	Amortization Period (Years)

Definite lived intangible assets:			
Key money store leases	$ 500	$ 124	Life of lease
Lease rights	665	210	Life of lease
Total	1,165	334	
Accumulated Amortization	(103)	(9)	
Total	$ 1,062	$ 325	

Key money is the amount of funds paid to a landlord or tenant to acquire the rights of tenancy under a commercial property lease for a certain property. Key money represents the right to lease with an automatic right of renewal. This

FS-48

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

right can be subsequently sold by the Company or can be recovered should the landlord refuse to allow the automatic right of renewal to be exercised. Key money is amortized over the respective lease terms.

Lease rights are costs incurred to acquire the right to lease a specific property. A majority of lease rights are related to premiums paid to landlords. Lease rights are recorded at cost and are amortized over the estimated useful term of the respective leases. Property lease terms are generally for 10 years.

Aggregate amortization expense of other definite lived intangible assets included in the Consolidated Statements of Operations under the caption General and administrative expenses for the years ended December 31, 2006 and 2005 was approximately $75 and $9, respectively. Assuming no changes in the Company s definite lived intangible assets, estimated amortization expense for each of the five succeeding fiscal years is as follows:

For the Years Ending December 31,	
2007	$ 123
2008	123
2009	123
2010	123
2011	123

NOTE 8 Other Assets

The components of other assets at December 31 are as follows:

	2006	**2005**
Lease security deposits	$ 4,934	$ 3,441
Worker s Compensation deposit	1,455	
Other	284	240
Total	$ 6,673	$ 3,681

NOTE 9 Accrued Expenses

The components of accrued expenses at December 31 are as follows:

	2006	**2005**
Accrued compensation and related taxes	$ 2,565	$ 2,466
Worker s Compensation self-insurance reserves	2,787	1,589

Sales taxes, value added tax, property taxes	1,373	724
Other	3,210	5,253
Total	$ 9,935	$ 10,032

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

NOTE 10 Long-term Bank Debt

Long-term bank debt at December 31 consists of the following:

	2006	2005
Credit Line Facility		
Revolving Credit Facility, maturing January 2010 (a)	$ 48,568	$ 41,925
Term Loans and Notes Payable		
Term loan with bank, maturing September 2007 (b)	3,750	4,167
Term loan with bank, maturing March 2010 (b)	1,872	
Term loan with bank, maturing October 2007 (c)	52	120
Term loan with bank, maturing December 2008 (c)	391	400
Various notes payable (d)	224	794
Leasehold improvement note, maturing March 2010 (e)	114	143
Leasehold improvement note, maturing April 2007 (e)	958	1,026
	7,361	6,650
Total Long-Term Bank Debt	55,929	48,575
Less current portion of bank debt	3,201	5,612
Long-Term Bank Debt, net of current portion	$ 52,728	$ 42,963

(a) At December 31, 2006 and 2005, the revolving credit facility with a bank provided for borrowings up to $57,500 and $55,000, respectively. Borrowings under the facility were subject to certain advance provisions established by the bank and were collateralized by all assets of the Company. Interest under the agreement was at LIBOR (5.30% and 4.84% at December 31, 2006 and 2005, respectively) plus 2.5% or the bank s prime rate (8.25% and 7.25% at December 31, 2006 and 2005, respectively) plus 2.25%, at the Company s option. The interest rate was 10.5% and 9.5% at December 31, 2006 and 2005, respectively. The facility was to expire in January 2010. The average borrowings during the years 2006 and 2005 were $46,500 and $38,663, respectively. Stockholders of the Company personally guaranteed the borrowings. On January 18, 2007, the Company negotiated an increase in the size of its credit facility from $57,500 to $62,500. Among other requirements, this facility agreement included a subjective acceleration clause and required the Company to maintain a lock box. As of December 31, 2006 and 2005 the Company was not in compliance with certain financial ratio covenants. As disclosed in Note 22, during July 2007, the Company replaced this revolving credit facility and converted this obligation into long-term debt with an increased revolving credit facility from another bank which expires at the earlier of July 2, 2012 or thirty days prior to the maturity date of the loan agreement with the private investment firm (January 18, 2009) unless it is refinanced on terms acceptable to the bank in December 2008. No charges for early extinguishment of debt were incurred associated with this transaction. As a result of the terms of the new credit agreement, the Company is currently in compliance with the covenants of the new agreement and accordingly, the loan balance at December 31, 2006 and 2005 is classified as a long-term obligation.

(b) At December 31, 2006 and 2005, the Company had a term loan with a bank. The loan is payable in monthly installments of $417, including interest at prime (8.25% and 7.25% at December 31, 2006 and 2005, respectively) plus 1% through September 2007. The balance at December 31, 2006 and 2005 was $3,750 and $4,167, respectively. At December 31, 2006, the Company had another term loan payable in monthly installments of $48, including interest at prime plus 1% through March 2010. The balance at December 31, 2006 was $1,872. Both of these loans were secured by various unsecured equipment. On January 18, 2007, the Company completed a $41 million secured debt financing with a private investment firm (see Note 22) and converted these obligations into long-term and accordingly, a portion of such debt was classified as

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

long-term. A portion of the financing proceeds was used to pay off both of these loans without any prepayment penalty. No charges for early extinguishment for debt were incurred associated with this transaction.

(c) At December 31, 2006 and 2005, the Company had two term loans with a financial institution. The first loan is payable in monthly installments of $5, including interest at prime (8.25% and 7.25% at December 31, 2006 and 2005, respectively) plus 1% through October 2007. The balance at December 31, 2006 and 2005 was $52 and $120, respectively. The second loan is payable in monthly installments of $22, including interest at prime plus 1% through December 2008. The balance at December 31, 2006 and 2005 was $391 and $400, respectively. Both of these loans are secured by related equipment, with a net book value of $520 and $552, respectively.

(d) At December 31, 2006 and 2005, the Company had various promissory notes payable in monthly installments aggregating $24, including interest ranging from 4.6% to 11.9% and maturing at various dates through August 2011. The notes are collateralized by equipment.

(e) At December 31, 2006 and 2005, the Company had two leasehold improvement term loans. The first loan is payable in monthly installments of $3 through March 2010, including interest at a rate of 8%. The balance at December 31, 2006 and 2005 was $114 and $143, respectively. The second loan is payable in monthly interest only payments at 9% through April 2007. The balance at December 31, 2006 and 2005 was $958 and $1,026, respectively.

Required principal payments of long-term debt (as adjusted to reflect the subsequent refinancing of long term debt disclosed in Note 23.) are as follows:

Year Ending December 31,	
2007	$ 3,201
2008	48,806
2009	3,899
2010	17
2011	6
	$ 55,929

NOTE 11 Notes Payable to Unrelated Parties

Unsecured notes payable to certain unrelated individuals are due upon demand with interest ranging from 10% to 24% per annum. The balance outstanding at December 31, 2006 and 2005 is $6,259 and $2,840, respectively, which is personally guaranteed by a stockholder.

NOTE 12 Notes Payable to Related Parties

Unsecured notes payable to certain individuals related to a stockholder are due upon demand with interest ranging from 12% to 18% per annum. The balance outstanding at December 31, 2006 and 2005 is $2,391 and $888, respectively.

NOTE 13 Subordinated Notes Payable to Unrelated Party

The Company has a financing agreement for borrowings of $12,500 with an unrelated third party, (the current second lien lender). Interest on the loan is at a rate of 17%. The Company pays monthly interest

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

payments at a rate of 11% on the current outstanding principal balance. The remaining unpaid portion of all monthly interest shall be added to the principal balance. The balance outstanding at December 31, 2006 and 2005 was $14,201 and $13,376, respectively, which includes accrued interest aggregating $1,701 and $876 at December 31, 2006 and 2005, respectively. On January 18, 2007, the Company completed a $41 million secured debt financing with a private investment firm and converted this obligation into long term debt (Note 22). Such amounts have been classified as long-term since they were refinanced on a long-term basis. A portion of the financing proceeds was used to pay off this loan plus the accrued interest without any prepayment penalty. No charges for early extinguishment for debt were incurred associated with this transaction.

This note was subordinated to the bank (Note 10). The agreement contained default and covenant provisions similar to its current bank agreement. At December 31, 2006 and 2005, the Company was not in compliance with certain financial ratio covenants. However, as a result of the refinancing on January 18, 2007 with a new long-term obligation, the subordinated notes payable is classified as a long-term liability.

NOTE 14 Subordinated Notes Payable to Related Parties

The Company has unsecured notes payable with a related party (relative of a stockholder), which are due upon demand with interest at 18%. The balance outstanding at December 31, 2006 and 2005 was $180. The note was subordinated to the interest of the bank which held the Company s revolving credit facility at December 31 2006 and 2005 as well as the interest of the bank which provided the new secured revolving credit facility on July 2, 2007 (see note 22).

The Company has an unsecured note payable to a stockholder which is due on demand with interest at 12%. The balance outstanding at December 31, 2006 and 2005, was $180. The note is subordinated to the interest of the bank which held the Company s revolving credit facility at December 31 2006 and 2005 as well as the interest of the bank which provided the new secured revolving credit facility on July 2, 2007 (see note 22).

NOTE 15 Capital Lease Obligations

The Company leases certain equipment under capital lease arrangements expiring at various times through 2011. The assets and liabilities under capital leases are recorded at the lower of the present values of the minimum lease payments or the fair values of the assets.

Minimum future payments under these capital leases are:

Year Ending December 31,	
2007	$ 3,397
2008	2,138
2009	989
2010	364
2011	101
Total future minimum lease payments	6,989
Less: amounts representing interest	(1,000)
Net minimum lease payments	5,989
Current portion	2,911

Long-term portion	$ 3,078

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

The interest rates pertaining to these capital leases range from 3.3% to 22.5% (average interest rate is 13.0%).

NOTE 16 Related Party Transactions

In December 2005, the Company entered into an operating lease, which commenced on November 15, 2006, for its knitting facility with a related company, which is partially owned by the stockholders of the Company. The monthly lease payments are $48 and the lease expires in November 2011, with a five year extension, at the option of the Company.

NOTE 17 Income Taxes

Income tax expense (benefit) for the years ended December 31, 2006 and 2005 consists of:

	2006	2005
State		
Current	$ 328	$ 239
Deferred	(348)	
Total	(20)	239
Foreign		
Current	1,355	$ 153
Deferred		
Total	$ 1,355	$ 153
Total	$ 1,335	$ 392

Income tax expense differs from the amount computed by applying the federal statutory tax rate of 34% to (loss) income before income taxes as shown below:

	2006	2005
Computed expected income tax (benefits) expense	$ (700)	$ 1,352
Reduced Federal tax rate for S Corporations	700	(1,352)
State income taxes, net of Federal income tax benefit	(20)	239
California enterprise zone tax credits	(2,833)	(2,833)
Change in valuation allowance	2,833	2,833
Foreign taxes	1,355	153
Income Tax Expense	$ 1,335	$ 392

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

The tax effects of temporary differences that give rise to deferred tax assets and deferred tax liabilities at December 31, 2006 and 2005 are presented below:

	2006	2005
Deferred tax assets:		
Allowance for doubtful accounts	$ 50	$ 26
Deferred rent	124	69
Accrued worker s compensation	57	10
Inventory capitalization for tax purposes	42	34
Inventory reserve	121	
Accrued liabilities	14	8
California enterprise zone tax credit	6,963	4,130
Total gross deferred tax assets	7,371	4,277
Less valuation allowance	(6,963)	(4,130)
Net deferred tax assets	408	147
Deferred tax liabilities:		
Prepaid expenses	(56)	(28)
Fixed assets	(16)	(119)
Total gross deferred tax liabilities	(72)	(147)
Net deferred tax assets and liabilities	$ 336	$

At December 31, 2006 and 2005, the Company had available state tax credit carryforwards of $6,963 and $4,130, respectively that may be utilized to offset future California state tax attributable to the tax on income earned if any, within a particular designated Enterprise Zone. These credits do not expire.

Management believes that it is more likely than not that the Company will realize the benefits related to these deductible temporary differences, except for the benefit to be derived from the utilization of the California Enterprise Zone tax credits. Consequently, the Company has provided a valuation allowance of $6,963 and $4,130 for the years ended December 31, 2006 and 2005, respectively.

NOTE 18 Commitments and Contingencies

Operating Leases

The Company conducts retail operations under operating leases, which expire at various dates through 2020. Future minimum rental payments, including related party lease (Note 16) (excluding real estate tax and maintenance costs) for retail locations and other leases that have initial or noncancelable lease terms in excess of one year at December 31, 2006 are as follows for the years ending December 31:

2007	$ 25,284
2008	24,345
2009	20,315
2010	17,862
2011	16,579
Thereafter	59,069
Total	$ 163,454

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

Operating lease rent expense (including real estate taxes and maintenance costs) and leases on a month to month basis were approximately $26,316 and $14,994 for the years ending December 31, 2006 and 2005, respectively. The Company did not incur any contingent rent during the same periods. Rent expense is included in cost of sales and general and administrative expenses in the accompanying Consolidated Statements of Operations.

Sales Tax

The Company has been contacted by the California State Board of Equalization in regard to scheduling a Sales and Use Tax audit for the period January 1, 2002 through December 31, 2004. No provision has been made for any future assessment, if any, which might be determined by the State Board of Equalization at the outcome of the audit.

California Franchise Tax Board

The Company has been contacted by the California Franchise Tax Board in regard to scheduling an audit related to California Enterprise Zone Tax Credits taken by the Company for the 2001 and 2002 income tax years. At this time no determination can be made as to the outcome of the audit and therefore no provision has been made for future assessment, if any, which might be determined by the California Franchise Tax Board as the outcome of the audit. However, the California Enterprise Zone Tax Credits have a full valuation allowance at December 31, 2006 and 2005 (Note 17).

Internal Revenue Service

The Company has been contacted by the Internal Revenue Service in regard to performing an audit for the income tax year 2005. The audit commenced in 2007. At this time no determination can be made as to the outcome of the audit and therefore no provision has been made for additional future assessment, if any, which might be determined by the Internal Revenue Service as the outcome of the audit.

Advertising

The Company has approximately $1,963 in open advertising commitments at December 31, 2006, which primarily relates to print advertisements in various newspapers and magazines during 2007.

NOTE 19 Workers Compensation Self-Insurance Reserves

Self Insurance Reserves

The Company uses a combination of third-party insurance and/or self-insurance for a number of risks including workers compensation and general liability claims. General liability costs relate primarily to litigation that arises from store operations. Self-insurance reserves include estimates of both claims filed carried at their expected ultimate settlement value and claims incurred but not yet reported. The Company s estimated claim amounts are discounted using a rate with a duration that approximates the duration of the Company s self-insurance reserve portfolio. The Company s liability reflected on the Consolidated Balance Sheet represents an estimate of the ultimate cost of claims incurred as of the balance sheet date. In estimating this liability, the Company utilizes loss development factors based on Company-specific data to project the future development of incurred losses. Loss estimates are adjusted based upon actual claim settlements and reported claims. These projections are subject to a high degree of variability based upon future inflation rates, litigation trends, legal interpretations, benefit level changes and claim settlement patterns. Although the Company does not expect the

FS-55

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

amounts ultimately paid to differ significantly from its estimates, self-insurance reserves could be affected if future claim experience differs significantly from the historical trends and the assumptions applied.

The workers compensation liability is based on the insurance company s estimate of losses for claims incurred, but not paid at year end. Funding is made directly to the providers and/or claimants by the insurance company. To guarantee performance under the workers compensation program, the Company has issued standby letters of credit in the amount of $3,256 in 2006 and 2005, with the insurance companies being the beneficiary, through its bank along with cash deposits of $1,455 and $0 as of December 31, 2006 and 2005, respectively. At December 31, 2006 and 2005, the Company recorded a reserve of $2,787 and $1,589, respectively, for potential losses on existing claims as such amounts are believed to be probable and reasonably estimable.

NOTE 20 Business Segment and Geographic Area Information

Segment Information

The Company s management reporting system evaluates performance based on a number of factors; however, the primary measures of performance are the net sales and income or loss from operations of each segment, as these are the key performance indicators reviewed by management. Operating income or loss for each segment does not include corporate general and administrative expenses, interest expense and other miscellaneous income/expense items. Corporate general and administrative expenses include, but are not limited to: human resources, legal, finance, IT and various other corporate level activity related expenses. Such unallocated expenses remain within corporate. The accounting policies of all operating segments are the same as those described in the summary of significant accounting policies in Note 2.

The Company reports the following segments: US Wholesale, US Retail and All Other. All of the Company s sales fall into one of these segments. The US Wholesale consists of sales of undecorated apparel products made to third party embellishers and other apparel manufacturers directly as well as through distributors including sales to its Canadian Affiliate that operated 25 and 20 retail stores at December 31, 2006 and 2005, respectively, plus wholesale operations. Internet sales are also recorded in the US wholesale segment. US Retail was comprised of 93 and 66 Company owned retail stores operating in the United States selling the Company s apparel products directly to consumers as of December 31, 2006 and 2005, respectively. The All Other segment comprises the international subsidiaries in Israel, continental Europe, the United Kingdom, Mexico, Japan and Korea, which operated 31 and 18 retail stores along with wholesale operations as of December 31, 2006 and 2005, respectively. None of these individual foreign operations meet any of the quantitative thresholds for separate disclosure, as defined in SFAS No. 131, Disclosures About Segments of an Enterprise and Related Disclosures .

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

The following tables represent key financial information of the Company s business segments for the year ended December 31, 2006:

	US Wholesale	US Retail	All Other	Consolidated
Net sales to external customers	$ 138,056	$ 80,210	$ 46,425	$ 264,691
Income from operations	14,221	11,510	4,719	30,450
Depreciation and amortization	4,852	3,709	869	9,430
Capital Expenditures	4,288	8,589	2,355	15,232
Deferred rent expense	2	1,641	128	1,771
Reconciliation to Loss Before Income Taxes				
Consolidated Income from operations of reportable segments				$ 30,450
Corporate expenses				(21,150)
Interest expense				(10,797)
Other income				607
Foreign currency transaction gain				601
Consolidated Loss Before Income Taxes				$ (289)
Net sales by location of customer				
United States				$ 207,971
Germany				14,585
Canada				10,295
United Kingdom				10,031
Japan				6,499
Other foreign countries				15,310
Total Consolidated Net Sales				$ 264,691
Long-lived assets Property and equipment, net as of December 31, 2006				
United States				$ 36,618
Germany				1,782
Japan				1,241
Korea				661
United Kingdom				974
France				875
Other foreign countries				318
Consolidated Long-lived Assets				$ 42,469
Identifiable assets by segment as of December 31, 2006				
US wholesale				$ 107,123
US retail				30,411
All other				10,623

Total	$	148,157

Foreign subsidiaries accounted for the following percentages of assets and total liabilities as of December 31, 2006:

Total assets	7%
Total liabilities	4%

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

Product Revenue for the year ended December 31, 2006

Net sales by class of customer:	
Wholesale	$ 149,396
Retail	115,295
Total Consolidated Net Sales	$ 264,691

The following table represents key financial information of the Company s business segments for the year ended December 31, 2005:

	US Wholesale	US Retail	All Other	Consolidated
Net sales to external customers	$ 128,274	$ 45,532	$ 14,300	$ 188,106
Income from operations	22,156	6,757	(806)	28,107
Depreciation and amortization	3,828	1,245	297	5,370
Capital Expenditures	2,695	9,667	2,273	14,635
Deferred rent expense	459	4,376	38	4,873
Reconciliation to Loss Before Income Taxes				
Consolidated Income from operations of reportable segments				$ 28,107
Corporate expenses				(17,872)
Interest expense				(6,258)
Other income				356
Foreign currency transaction loss				(358)
Consolidated Income Before Income Taxes				$ 3,975
Net sales by location of customer				
United States				$ 157,240
Germany				14,585
Canada				10,850
United Kingdom				4,167
Japan				420
Other foreign countries				844
Total Consolidated Net Sales				$ 188,106
Long-lived assets Property and equipment, net as of December 31, 2005				
United States				$ 29,970
Germany				1,361
Japan				1,014
Korea				217

United Kingdom		718
Other foreign countries		195
Consolidated Long-lived Assets	$	33,475
Identifiable assets by segment as of December 31, 2005		
US wholesale	$	103,537
US retail		17,563
All other		3,126
Total	$	124,226

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

Foreign subsidiaries accounted for the following percentages of assets and total liabilities as of December 31, 2005:

Total assets	3%
Total liabilities	2%

Product Revenue for the year ended December 31, 2005

Net sales by class of customer:	
Wholesale	$ 128,274
Retail	59,832
Consolidated Net Sales	$ 188,106

NOTE 21 Litigation

The Company is subject to various claims and contingencies in the ordinary course of its business, including those related to litigation, business transactions, employee-related matters and taxes, among others. When the Company is aware of a claim or potential claim, it assesses the likelihood of any loss or exposure. If it is probable that a loss will result and the amount of the loss can be reasonably estimated, the Company will record a liability for the loss. The liability recorded includes probable and estimable legal costs associated with the claim or potential claim. If the loss is not probable or the amount of the loss cannot be reasonably estimated, the Company discloses the claim if the likelihood of a potential loss is reasonably possible and the amount involved could be material.

The Company is currently involved in matters with a few ex-employees who have either filed claims or state intentions to file various claims against the Company with the courts and regulatory agencies, which relate to alleged labor law violations, sexual harassment and other vague employment claims. One such claim against the Company was filed during 2005. During 2006, the Company was notified by two other ex-employees with respect to potential claims against the Company. One of these two ex-employees filed their claim against the Company in 2007. Since these matters are currently in discovery or still in the early stages, no determination can be made at this time as to their final outcome, nor can the range of potential loss be estimated.

During 2006, a complaint was also filed against the Company by a customer who is claiming that the Company improperly recorded personal information at the point of sale at one of the Company s retail locations. Since this matter is currently in discovery and still in the early stages, no determination can be made at this time as to its final outcome, nor can the range of potential loss be estimated.

The above mentioned complaints seek unspecified judgments and attorney s fees and costs. Although the outcome of such items cannot be determined with certainty, the Company is of the opinion that the final outcome of these matters are either without merit or will not have a material adverse impact on its consolidated financial position or results of operations. Management intends to defend itself vigorously against the allegations in these complaints.

NOTE 22 Subsequent Events

On December 18, 2006, the Company signed a definitive Acquisition Agreement with Endeavor, a blank check company publicly listed on the American Stock Exchange. Upon consummation of the merger, the

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

Company would become a wholly-owned subsidiary of Endeavor. However, since one of the stockholders of the Company would own a majority of the outstanding common stock of Endeavor, the merger is expected to be accounted for as a reverse acquisition. For accounting purposes, the transaction would be accounted for as a recapitalization of the Company. As part of the merger, the Canadian Affiliate is also being acquired by Endeavor.

The merger is subject to customary closing conditions, and is expected to close in the second half of 2007. As part of the agreement, the Company is required to achieve certain financial targets set forth in the agreement. While the Company was not in compliance with the financial targets, in April 2007 Endeavor waived the requirements to comply with certain financial targets. The Company and Endeavor can terminate the agreement at any time if mutually agreed. The agreement will terminate if a closing does not occur by December 15, 2007, and is subject to the approval of Endeavor s stockholders. There can be no assurances that the merger will be completed.

On January 18, 2007, the Company completed a $41 million secured debt financing with a private investment firm. The proceeds of the financing were used to repay the Company s subordinated notes payable with it current second lien holder (Note 13) of $15,000 (including principal, interest and fees), and repay its term loans with its bank (Note 10) of $5,600. No charges for early extinguishment of debt were incurred associated with payoff of these notes. Net proceeds related to the secured debt financing amounted to approximately $18 million. Indebtedness under the agreement bears interest at 16% per annum, payable monthly and matures on January 18, 2009. The agreement requires the Company to comply with certain covenants. In the event the Company is in default under the agreement the interest rate increases to 21% per annum and the private investment firm has the right to demand payment in full of all outstanding indebtedness. The agreement does not allow any prepayments prior to January 18, 2008 and subsequent to that date, any prepayment shall include a prepayment premium equal to 3% of the amount prepaid. The Company is currently in compliance with these covenants.

On July 2, 2007, the Company obtained an additional $10 million secured debt financing with the same private investment firm under the same terms as the original agreement on January 18, 2007. As of June 30, 2007 the Company was in violation of certain covenants of the original agreement from January 18, 2007. However, the default was subsequently waived and covenants were amended by the lender at the time of the additional financing obtained July 2, 2007.

On July 2, 2007, the Company also replaced its secured revolving credit facility of $62,500 (Note 10) with an increased revolving credit facility of up to $75,000 from a new bank. The Company did not incur any losses for early extinguishment of debt with this transaction. Prepayment fees of $313 were expensed in July 2007. Borrowings under the facility are subject to certain advance provisions established by the bank and are collateralized by all assets of the Company. Interest under the agreement is at LIBOR plus 2% or the Prime rate, at the Company s option. The credit facility expires at the earlier of July 2, 2012 or thirty days prior to the maturity date of the loan agreement with the private investment firm (January 18, 2009) unless it is refinanced on terms acceptable to the bank. The credit facility agreement requires the Company to comply with certain covenants. The Company is currently in compliance with these covenants.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

(Dollars in thousands)

For the Years Ended December 31, 2006 and 2005

NOTE 23 Reclassification

The Company has reclassified its previously issued December 31, 2006 and 2005 consolidated financial statements for certain operating expenses. This reclassification predominantly related to certain store retail rents that were previously included in General and Administrative which have been reclassified to Selling. The reclassification had no effect on the consolidated balance sheets, the statements of stockholders equity or reported net (loss) income for any period.

The effect on the Company s previously issued 2006 and 2005 financial statements is summarized as follows:

Statement of Operations for the Year Ended December 31, 2006

	Previously Reported	Increase (Decrease)	As Reclassified
Selling	49,321	24,185	73,506
Warehouse and Distribution	6,669	12	6,681
General and Administrative	61,016	(24,197)	36,819

Statement of Operations for the Year Ended December 31, 2005

	Previously Reported	Increase (Decrease)	As Reclassified
Selling	34,496	11,277	45,767
Warehouse and Distribution	4,156	4	4,160
General and Administrative	38,171	(11,275)	26,896

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Balance Sheet

December 31, 2004

(unaudited)

ASSETS	
CURRENT ASSETS	
Cash	$ 2,065,145
Receivables	
Due from factor	361,986
Trade, net of allowances of $864,000	12,035,414
Due from Canadian affiliate	1,569,919
Prepaid expenses	163,654
Inventories	47,072,327
Total current assets	63,268,445
PROPERTY AND EQUIPMENT, net	17,765,209
DEPOSITS	1,831,006
Total assets	$ 82,864,660
LIABILITIES AND STOCKHOLDERS EQUITY	
CURRENT LIABILITIES	
Cash overdraft	$ 1,301,452
Line of credit	31,705,437
Accounts payable	15,884,356
Accrued expenses	3,136,490
Income taxes payable	117,970
Notes payable to unrelated parties	2,074,432
Notes payable to related parties	763,945
Current Portion of long-term obligations	2,277,428
Subordinated notes payable to related parties	360,000
Total current liabilities	57,621,510
TERM LOAN, net of current position	423,917
CAPITAL LEASE OBLIGATIONS, net of current position	2,689,124
LONG-TERM DEBT, net of current position	724,411
DEFERRED RENT	1,365,406
SUBORDINATED NOTE PAYABLE	7,577,666
Total liabilities	70,402,034
COMMITMENTS AND CONTINGENCIES	
STOCKHOLDER S EQUITY	
Common stock, no par value, 1,000,000 shares authorized, 100,000 shares issued and outstanding	300
Additional paid-in-capital	5,706,034
Due from stockholders	(1,197,334)
Retained earnings	7,953,626
Total stockholder s equity	12,462,626

Total Liabilities and Stockholders Equity	$ 82,864,660

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

FS-62

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statement of Income

For the Year Ended December 31, 2004

(unaudited)

NET SALES (including sales to Canadian affiliate of $9,223,000)	$ 127,928,668
COST OF SALES (including cost of sales for the Canadian affiliate of $1,473,000)	80,994,988
Gross profit	46,933,680
OPERATING EXPENSES (Reclassified see Note 22)	
Selling	19,547,481
Warehouse and distribution	4,061,143
General and administrative	14,066,445
	37,675,069
Income from operations	9,258,611
INTEREST AND OTHER (INCOME) EXPENSE	
Interest expense	1,927,613
Foreign currency transaction gain	(351,978)
Other expense	340,405
	1,916,040
INCOME BEFORE INCOME TAXES	7,342,571
INCOME TAX PROVISION	1,019,139
NET INCOME	$ 6,323,432

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

FS-63

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statement of Stockholders Equity

December 31, 2004

(unaudited)

	Preferred Stock, no par value, 100,000 shares authorized (Note 19)		Common Stock, no par value, 1,000,000 shares authorized					
	Outstanding shares	Amount	Outstanding shares	Amount	Additional Paid-in Capital	Due from Stockholders	Retained Earnings	Stockholders Equity
BALANCE, January 1, 2004	87,650	$ 5,001,408	100,000	$ 300	$	$	$ 1,943,061	$ 6,944,769
Cancellation redemption of preferred stock	12,350	704,626						704,626
Cancellation of preferred stock	(100,000)	(5,706,034)			5,706,034			
Advances to stockholders						(1,197,334)		(1,197,334)
Distributions to stockholders							(312,867)	(312,867)
Net income							6,323,432	6,323,432
BALANCE, December 31, 2004		$	100,000	$ 300	$ 5,706,034	$ (1,197,334)	$ 7,953,626	$ 12,462,626

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

FS-64

Table of Contents

American Apparel, Inc. and Subsidiaries

Consolidated Statement of Cash Flows

For the Year Ended December 31, 2004

(unaudited)

CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from customers	$ 121,976,189
Cash paid to suppliers, employees and others	(136,046,948)
Interest Paid	(1,927,613)
Income taxes paid	(521,831)
Other	(86,563)
Net cash used by operating activities	(16,606,766)
CASH FLOWS USED INVESTING ACTIVITIES	
Purchase of property and equipment	(9,895,714)
CASH FLOWS FROM FINANCING ACTIVITIES	
Change in matured funds from factor, net	(14,710,795)
Cash overdraft from financial institution	1,301,452
Borrowings under line of credit, net	31,705,437
Distributions to stockholders	(312,867)
Notes payable to related parties	477,741
Notes payable to unrelated parties	1,728,000
Repayment of notes payable to unrelated parties	(98,568)
Borrowing of term loan	200,000
Repayment of term loan	(143,422)
Borrowings of long-term debt	8,687,753
Repayment of long-term debt	(173,285)
Repayment of capital lease obligations	(412,355)
Advances to stockholders	(1,197,334)
Cancellation of redemption of redeemable preferred stock	704,626
Net cash provided by financing activities	27,756,383
NET CHANGE IN CASH	1,253,903
CASH, beginning of period	811,242
CASH, end of period	$ 2,065,145
RECONCILIATION OF NET INCOME TO NET CASH USED BY OPERATING ACTIVITIES	
Net income	$ 6,323,432
Depreciation and amortization	2,205,643
Provision for bad debt	1,365,998
Deferred income taxes	88,423
Deferred rent	1,365,406
Increase (decrease) in cash due to changes in operating assets and liabilities	
Receivables	(5,907,117)
Inventories	(26,437,889)
Prepaid expenses	127,915

Other assets	(1,665,356)
Accounts payable	5,267,523
Accrued expenses	250,371
Income taxes payable	408,885
	$ (16,606,766)

NON-CASH INVESTING AND FINANCING ACTIVITIES	
Property and equipment acquired under capital lease	$ 2,904,243

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

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

For the Year Ended December 31, 2004

(unaudited)

NOTE 1 Organization and Business

American Apparel, Inc. (AA), a California corporation is a vertically-integrated manufacturer, distributor and retailer of branded fashion basic apparel for men, women and children. AA sells its products through a wholesale distribution channel supplying t-shirts and other casual wear to distributors and screen printers, as well as direct to end users through its retail stores located in the United States and stores internationally. In addition, AA operates an online retail e-commerce website. AA, collectively with its subsidiaries is referred to as the Company .

The Company maintains its corporate offices, primary manufacturing and distribution facility, knitting and dye house in Los Angeles, California. The Company also maintains a portion of its yarn at outside knitting facilities and a portion of its greige goods at outside dye houses.

The wholly-owned operating subsidiaries of the Company are:

Sales

United States: American Apparel Retail, Inc. (AAR) operates retail stores. American Apparel Retail 1090 Third NYC, Inc., a wholly-owned subsidiary of AAR, operates a retail store in New York.

Continental Europe: American Apparel Deutschland GmbH operates retail stores and distributed American apparel products.

United Kingdom: American Apparel (Carnaby) Limited operates retail stores. American Apparel (UK) Limited distributes American Apparel products.

Manufacturing

KCL Knitting, LLC is engaged in textile manufacturing. The operating agreement under which KCL conducts its business provides that the term of their existence should continue until December 31, 2050.

NOTE 2 Summary of Significant Accounting Policies

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of American Apparel, Inc. and the following direct or indirect wholly-owned subsidiaries: American Apparel Retail, Inc., KCL Knitting, LLC, American Apparel Deutschland GmbH, American Apparel (UK) Limited, American Apparel (Carnaby) Limited, and American Apparel Retail 1090, Third NYC, Inc. All intercompany accounts and transactions have been eliminated upon consolidation.

Use of Estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under

FS-66

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The most significant estimates include; sales returns and other allowances, allowance for doubtful accounts, inventory valuation and obsolescence, valuation and recoverability of long-lived intangible assets including the values assigned to acquired assets, property and equipment, income taxes; and accruals for the outcome of current litigation.

On a continual basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews, and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates.

Revenue Recognition

The Company recognizes product sales revenue when title and risk of loss have transferred to the customer, there is persuasive evidence of an arrangement, shipment and passage of title has occurred, the sales price is fixed or determinable and collectibility is reasonably assured. Revenue from wholesale product sales and on-line product sales are recorded at the time the product is shipped to the customer. With respect to its own retail store operations, the Company recognizes revenue upon the sale of its products to retail customers. The Company s net sales represent gross sales invoiced to customers, less certain related charges for discounts, returns, and other promotional allowances. Allowances provided for these items are presented in the consolidated financial statements primarily as reductions to sales and cost of sales (see Sales Returns and Other Allowances discussed below for further information).

The Company recognizes the sales from gift cards, gift certificates and store credits as they are redeemed for merchandise. Prior to redemption, the Company maintains an unearned revenue liability for gift cards, gift certificates and store credits until the Company is released from such liability. The Company s gift cards, gift certificates and store credits do not have expiration dates. The unearned revenue for gift cards, gift certificates and store credits are recorded in accrued expenses in the amount of $79,285 at December 31, 2004.

Sales Returns and Other Allowances

Allowances For Sales Returns The Company analyzes sales returns in accordance with Statement of Financial Accounting Standard (SFAS) No. 48 Revenue Recognition When Right of Return Exists (SFAS 48). The Company is able to make reasonable and reliable estimates of product returns for its wholesale, on-line product sales and retail store sales based on the Company s past history. The Company also monitors the buying patterns of the end-users of its products based on sales data received by its retail outlets. Estimates for sales returns are based on a variety of factors including actual returns and based on expected return data communicated to it by customers. Accordingly, the Company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates.

As with any set of assumptions and estimates, there is a range of reasonably likely amounts that may be calculated for each allowance above. However, the Company believes that there would be no significant difference in the amounts reported using other reasonable assumptions than what was used to arrive at each allowance. The Company regularly reviews the factors that influence its estimates and, if necessary, makes adjustments when it believes that actual product returns, credits and other allowances may differ from established reserves. Actual experience associated with any of these items may be significantly different than the Company s estimates.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to credit risk consist primarily of cash (the amounts of which may, at times, exceed Federal Deposit Insurance Corporation limits on insurable amounts) and trade accounts receivable, relating substantially to the Company s wholesale segment. The Company mitigates its risk by investing in or through major financial institutions. The Company has approximately $467,000 held in foreign banks at December 31, 2004.

The Company performs on-going credit evaluations of its customers and adjusts credit limits based upon payment history and the customer s current credit worthiness, as determined by the review of their current credit information. Collections and payments from customers are continuously monitored. The Company maintains an allowance for doubtful accounts, which is based upon historical experience as well as specific customer collection issues that have been identified. While such bad debt expenses have historically been within expectations and allowances established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Cash

The Company s cash balances represent cash on deposit held at banks.

Inventories

Inventories are stated at the lower of cost or market. Cost is primarily determined on the first-in, first out (FIFO) method. The cost elements of inventories include materials, labor and overhead. During 2004 no one supplier provided more than 10% of the Company s raw material purchases.

The Company identifies potentially excess and slow-moving inventories by evaluating turn rates, inventory levels and other factors. Excess quantities are identified through evaluation of inventory agings, review of inventory turns and historical sales experiences. The Company provides lower of cost or market reserves for such identified excess and slow-moving inventories.

To account for inventory shrinkage, the Company establishes a reserve as an estimate based upon the analysis of inventory amounts on hand at segments for which quarterly physical inventories are not performed.

Property and Equipment

Property and equipment are carried at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of the related assets. The costs of normal maintenance and repairs are charged to expense in the year incurred. Expenditures which significantly improve or extend the life of an asset are capitalized and depreciated over the asset s remaining useful life. Amortization of leasehold improvements is computed using the straight-line method over the shorter of the estimated useful lives of the related assets or the lease term. Upon sale or disposition, the related cost and accumulated depreciation are removed from the accounts and the resulting gain or loss, if any, is reflected in operations.

Impairment of Long-Lived Assets

The Company follows the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144). SFAS 144 requires evaluation of the need for an impairment charge relating to long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The estimated future undiscounted cash flows associated with the asset would be

compared to the asset s carrying amount to determine if a write down to a new depreciable basis is required. If required, an impairment charge is recorded based on an estimate of future discounted cash flows.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

Foreign Currency

The financial statements of international subsidiaries are translated into U.S. Dollars using the exchange rate at each balance sheet date for assets and liabilities and an average exchange rate for each period for revenues, expenses, gains and losses. Foreign currency transaction gains and losses are charged or credited to operations as incurred. Where the local currency is the functional currency (which is determined based on management s judgment and involves consideration of all relevant economic facts and circumstances affecting the subsidiary) translation adjustments are recorded as a separate component of stockholders equity. During fiscal 2004, the Company recognized foreign currency transaction gains of $351,978.

Income Taxes

The Company elected Subchapter S corporation status effective July 1, 2004. Consequently, the Company eliminated the previously reported deferred tax assets and liabilities, which resulted in recording an income tax benefit. Earnings and losses for Federal tax reporting purposes are included in the personal tax returns of the stockholders and taxed according to their personal tax strategies. Accordingly, the Company does not incur Federal income tax obligations, and the consolidated financial statements do not include a provision for Federal income taxes. The Company expects to distribute the amounts necessary to satisfy the stockholders estimated personal income tax liabilities based upon the Company s taxable income. State taxes are provided at applicable statutory rates multiplied by pre-tax income. The Company has Enterprise Zone credits available to offset current tax liabilities.

American Apparel Deutschland GmbH, American Apparel UK (Limited) and American Apparel (Carnaby) are foreign domiciled entities subject to foreign income taxes on earnings in the respective jurisdictions. For the year ended December 31, 2004, no foreign tax provision was recorded. A valuation allowance of approximately $200,000 was recorded against losses incurred by the German subsidiary.

KCL Knitting, LLC (KCL) is a limited liability company, classified as a pass-through entity for federal income tax purposes, which provides for profits and losses to be reported by American Apparel, Inc.

American Apparel, Inc. has unrecognized built-in gains of approximately $26 million resulting from its S corporation election. If any of the assets creating the unrecognized built-in gains are sold in the ten year period ending July 1, 2014, AA is liable for Federal income taxes on those gains. The gain is determined by using the tax basis of the assets compared with the fair value of those assets at the time of the S corporation election. No deferred income taxes have been provided as the built-in gain relates primarily to intangible assets that are not expected to be sold within the ten year holding period.

Fair Value of Financial Instruments

The Company s financial instruments include cash, accounts receivable, accounts payable, revolving line of credit, and long-term debt. The Company estimates that carrying amounts of all financial instruments described above to approximate fair value based upon current market conditions, maturity dates, and other factors.

Advertising, Promotion and Catalog

The Company expenses the production costs of advertising the first time the advertising takes place. The advertising expenses for the year ended December 31, 2004 amounted to $2,322,912 and was included in selling expense in the Consolidated Statement of Income.

FS-69

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

Shipping and Handling Costs

The Company incurs shipping and handling costs in its operations. These costs, included in cost of sales in the Consolidated Statement of Income. Shipping and handling costs billed to customers amounted to $2,546,935 and is included in Net Sales for the year ended December 31, 2004.

Deferred Rent, Rent Expense and Tenant Allowances

The Company occupies its retail stores and combined corporate office, manufacturing, and distribution center under operating leases generally with terms of one to ten years. Some leases contain renewal options for periods ranging from five to fifteen years under substantially the same terms and conditions as the original leases. Most of the store leases require payment of a specified minimum rent, a contingent rent based on a percentage of the store s net sales in excess of a specified threshold, plus defined escalating rent provisions. The Company straight-lines and recognizes its rent expense over the term of the lease (including probable lease renewals), plus the construction period prior to occupancy of the retail location, using a mid-month convention. Also included in rent expense are payments of real estate taxes, insurance and certain common area and maintenance costs in addition to the future minimum operating lease payments. All other pre-opening costs are expensed as incurred.

Start-up Costs

The Company expenses as incurred all retail store start-up and organization costs, including travel, training, recruiting, salaries and other operating costs.

Self-insurance accruals

The Company self-insures a significant portion of expected losses under its workers compensation program. Accrued liabilities are recorded based on the Company s estimates of the ultimate costs to settle incurred claims, both reported and unreported.

New accounting standard

In November 2004, the Financial Accounting Standards Board issued SFAS No 151, Inventory Costs An Amendment of Accounting Research Bulletin No. 43, Chapter 4 (SFAS 151). SFAS 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs and spoilage should be expensed as incurred and not included in overhead. The provisions of SFAS No. 151 must be applied prospectively to the Company s inventory costs incurred after January 1, 2006. The Company expects that the adoption will not have a material impact on its consolidated financial position or results of operations.

NOTE 3 Due from Factor

The Company has entered into a factoring agreement whereby it assigns a portion of its accounts receivable to a factor. The factor charges a commission on the net sales factored. The factor provides credit administration and assumes credit risk for all receivables assigned without recourse. Under inter-creditor agreements, the factored receivables are assigned to a bank (Note 7). Due from factor at December 31, 2004 consists principally of matured funds. Matured funds represent amounts due from the factor for cash collected from customers in excess of advances received.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

Included in accounts payable at December 31, 2004 is approximately $1,683,000 due to the factor for piece good purchases.

NOTE 4 Due from Stockholders

Unsecured advances to the stockholders bear interest at 2% per annum and are payable upon demand. The amounts due from the stockholders have been presented as deductions from stockholders equity in the financial statements.

NOTE 5 Inventories, net

The components of inventories are as follows:

	December 31, 2004
Raw materials	$ 13,886,177
Work in process	1,063,904
Finished goods	32,122,246
Total	$ 47,072,327

NOTE 6 Property and Equipment

The components of property and equipment are as follows:

	December 31, 2004	Depreciation and Amortization Period (Years)
Machinery and equipment	$ 11,244,313	5-7 years
Furniture and fixtures	2,278,762	5 years
Computers and software	3,587,513	3-5 years
Automobiles	65,659	3 years
Leasehold improvements	5,720,071	Shorter of the life of lease or useful life
Construction in progress	470,171	
	23,366,489	
Accumulated depreciation and amortization	(5,601,280)	
	$ 17,765,209	

Depreciation and amortization expense relating to property and equipment (including capitalized leases) was $2,205,643 for the year ended December 31, 2004. Property and equipment includes $5,568,689 for assets held under capital leases at December 31, 2004. Accumulated

amortization for these capital leases at December 31, 2004 was $1,300,566.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

NOTE 7 Line of Credit

The Company has a credit facility with a bank providing for borrowings up to $45,000,000. Borrowings under the facility are subject to certain advance provisions established by the bank and are collateralized by all assets of the Company. Interest under the agreement will be at LIBOR plus 3.0% or the bank s prime rate plus .5%, at the Company s option. At December 31, 2004, outstanding borrowings amount to $31,705,437. Stockholders of the Company personally guaranteed the borrowings up to a maximum of $2,000,000. The credit agreement is subject to various covenants relating to the maintenance of specific financial ratios. At December 31, 2004, the Company was not in compliance with certain financial ratio covenants. The Company received a waiver for the violations at December 31, 2004.

NOTE 8 Accrued Expenses

The components of accrued expenses are as follows:

	December 31, 2004
Sales tax payable	$ 214,540
Store credit	10,649
Gift certificates	68,636
Accrued expenses	1,486,563
Accrued salaries & wages and related taxes	947,102
Workers Compensation self-insurance reserves	409,000
	$ 3,136,490

NOTE 9 Notes Payable to Unrelated Parties

Unsecured notes payable to certain unrelated individuals are due upon demand with interest at 12% per annum.

NOTE 10 Notes Payable to Related Parties

Unsecured notes payable to certain individuals related to a stockholder are due upon demand with interest at 12% per annum.

NOTE 11 Term Loan

Term loan with a bank, payable in monthly installments of $12,500, including interest at prime plus 1% through September 2008. Loan is secured by related equipment	$ 550,000
Unsecured term loan with the Canadian Affiliate payable in monthly installments of $1,537, including interest at a rate of 11.99% per annum through May 2007	38,524
	588,524

Current portion	(164,607)
Long-term portion	$ 423,917

FS-72

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

Scheduled annual principal maturities for term loans are as follows:

Years ending December 31,	
2005	$ 164,607
2006	166,458
2007	157,459
2008	100,000
	$ 588,524

NOTE 12 Long-Term Debt

Various promissory notes, payable in monthly installments of $56,503 including interest ranging from 2.9% to 10.5% through November 2007. The notes are collateralized by equipment	$ 1,339,453
Current portion	(615,042)
Long-term portion	$ 724,411

Scheduled annual principal maturities for long-term debt are as follows:

Year ending December 31,	
2005	$ 615,042
2006	563,968
2007	160,443
	$ 1,339,453

NOTE 13 Capital Lease Obligations

The Company leases certain equipment under capital lease arrangements. Minimum lease payments for future years ending December 31, are as follows:

2005	$ 1,861,394
2006	1,553,598
2007	931,609

2008	482,214
2009	136,087
Total future minimum lease payments	4,964,902
Amount representing interest	(777,999)
Net of minimum lease payments	4,186,903
Current portion	(1,497,779)
Long-term portion	$ 2,689,124

Cost of equipment under capital leases and the related accumulated amortization amounted to $5,568,689 and $1,300,566 respectively, at December 31, 2004. Amortization expense amounted to $703,780 for the year ended December 31, 2004.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

NOTE 14 Subordinated Notes Payable

The Company has a financing agreement for borrowings of $7,500,000 with an unrelated third party. Interest on the loan is at a rate of 17% per annum, which commenced in November 2004. The Company pays monthly interest payments at a rate of 11% for the outstanding principal balance and accrued interest. On October 1, 2009, the Company must pay 50% of the outstanding principal balance of the loan, including all unpaid interest. On October 1, 2010, the Company must pay the entire remaining outstanding balance of the loan, including all unpaid interest.

During the first year of the financing agreement, the lender, has the discretion to make additional advances up to $5,000,000 to the Company. Advances shall be at least $1,000,000 and in increments of $1,000,000. On the fifth anniversary of an advance, the Company must pay the entire outstanding principal balance, including all accrued interest.

The Company paid the lender, a closing fee in the amount of $112,500 at the commencement of the financing agreement. The Company is obligated to pay the lender, a closing fee related to any advances in an amount of 1.5% of the balance.

The balance outstanding at December 31, 2004 was $7,577,666. The note is subordinated to the bank (Note 7). The agreement contains default and covenant provisions similar to the its bank agreement. At December 31, 2004, the Company was not in compliance with certain financial ratio covenants. The Company received a waiver for the violations at December 31, 2004.

NOTE 15 Subordinated Notes Payable to Related Parties

The Company has a revolving line of credit with a related party (relative of a stockholder), for borrowings up to $500,000. Borrowings on this line are secured by a lien on substantially all of the assets of the Company. The line bears interest at 12% and borrowings on the line are due on demand. The balance outstanding at December 31, 2004 is $180,000. Borrowings on this line of credit are subordinated to the interest of the bank.

The Company also has an unsecured note payable to a stockholder which is due on demand with interest at 12%. The balance outstanding at December 31, 2004 is $180,000. The note is subordinated to the interest of the bank.

NOTE 16 Related Party Transactions

The Company sold merchandise to the Canadian Affiliate amounting to approximately $9,223,000 during the year ended December 31, 2004. During the year ended December 31, 2004, the Company incurred expenses of approximately $1,473,000 for various goods and services provided by the Canadian Affiliate. Amounts due from the Canadian Affiliate amounted to approximately $1,569,000 at December 31, 2004.

NOTE 17 Commitments

The Company leases an operating facility and various retail stores under non-cancelable operating leases with expiration dates ranging from April 2005 to December 2015. In addition, the Company rents its main operating facility and other facilities, including warehouse space and showrooms under non-cancelable operating leases with expiration dates through December 31, 2008. The Company has an option for lease renewals for various retail stores. Most leases also provide for payment of operating expenses, real estate taxes and additional rent based on a percentage of sales. For the year ended December 31, 2004, the Company did not incur contingent rental expenses. Rent expense for the year ended December 31, 2004 amounted to $4,968,851.

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

Future minimum payments under the non-cancelable operating leases are as follows:

Years ending December 31,	
2005	$ 10,901,121
2006	11,982,407
2007	12,290,971
2008	12,333,454
2009	8,500,067
Thereafter	31,939,900
	$ 87,947,920

NOTE 18 Contingencies

The Company is from time to time, involved in litigation incidental to the conduct of its business. The Company believes that the outcome of such litigation will not have a material adverse effect on its results of operations or financial condition.

Sales tax

The Company has been contacted by the California State Board of Equalization in regard to scheduling a Sales and Use Tax audit for the period January 1, 2002 through December 31, 2004. No provision has been made for any future assessment, if any, which might be determined by the State Board of Equalization at the outcome of the audit.

NOTE 19 Preferred stock

On July 1, 2003, the Company issued 100,000 shares of its no par value Preferred Stock. At June 30, 2004 the unredeemed shares were canceled and converted into additional paid in capital.

NOTE 20 Workers Compensation Insurance

The Company maintains a self-insurance program for workers compensation. The liability is based on the insurance company s estimate of losses for claims incurred, but not paid at year-end. Funding is made directly to the providers and/or claimants by the insurance company. To guarantee performance under the workers compensation program, the Company has a standby letter of credit in the amount of $800,000, with the insurance company being the beneficiary. At December 31, 2004, the Company recorded a reserve of approximately $409,000 for potential losses on existing claims as such amounts are believed to be probable and reasonably estimable.

NOTE 21 Business Segment and Geographic Area Information

Segment Information

The Company s management reporting system evaluates performance based on a number of factors; however, the primary measures of performance are the net sales and income or loss from operations of each segment, as these are the key performance indicators reviewed by

management. Operating income or loss for each segment does not include corporate general and administrative expenses, interest expense and other miscellaneous income/expense items. Corporate general and administrative expenses include, but are not limited

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

to: human resources, legal, finance, IT and various other corporate level activity related expenses. Such unallocated expenses remain within corporate. The accounting policies of all operating segments are the same as those described in the summary of significant accounting policies in Note 2.

The Company reports the following segments: US Wholesale, US Retail and All Other. All of the Company s sales fall into one of these segments. The US Wholesale consists of sales of undecorated apparel products made to third party embellishers and other apparel manufacturers directly as well as through distributors including sales to its Canadian Affiliate that operates retail stores plus wholesale operations. Internet sales are also recorded in the US Wholesale segment. US Retail is comprised of Company owned retail stores operating in the United States selling the Company s apparel products directly to consumers. The All Other segment comprises the international subsidiaries in continental Europe and the United Kingdom, which operate retail stores along with wholesale operations. None of these individual foreign operations meet any of the quantitative thresholds for separate disclosure, as defined in SFAS No. 131, Disclosures About Segments of an Enterprise and Related Disclosures.

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(unaudited)

The following table represents key financial information of the Company s business segments for the year ended December 31, 2004:

	US Wholesale	US Retail	All Other	Consolidated
Net sales to external customers	$ 117,715,499	$ 7,810,382	$ 2,402,787	$ 127,928,668
Income from operations	9,531,766	910,833	(1,183,988)	9,258,611
Depreciation & amortization	1,913,332	220,763	71,548	2,205,643
Capital Expenditures	4,970,033	3,704,481	1,221,200	9,895,714
Deferred rent expense	918,524	446,093	789	1,365,406
Reconciliation to Income Before Income Taxes				
Consolidated Income from operations of reported segments				$ 9,258,611
Interest expense				(1,927,613)
Other expense				(340,405)
Foreign currency transaction gain				351,978
Consolidated Income Before Income Taxes				$ 7,342,571
Net sales by location of customer				
United States				$ 116,302,881
Canada				$ 9,223,000
United Kingdom				930,462
Other foreign countries				1,472,325
Total Consolidated Net Sales				$ 127,928,668
Long-lived assets Property & equipment as of December 31, 2004				
United States				$ 16,269,459
United Kingdom				743,920
Other foreign countries				751,830
Consolidated Long-lived Assets				$ 17,765,209
Identifiable assets by segment as of December 31, 2004				
US wholesale				$ 68,961,996
US retail				9,622,608
All other				4,280,056
Total				$ 82,864,660
Foreign subsidiaries accounted for the following percentages of assets & total liabilities as of December 31, 2004				
Total assets				5.2%
Total liabilities				7.7%

Product Revenue for the year ended December 31, 2004	
Net sales by class of customer	
Wholesale	$ 117,715,499
Retail	10,213,169
Consolidated Net Sales	$ 127,928,668

Table of Contents

American Apparel, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

For the Year Ended December 31, 2004

(Unaudited)

NOTE 22 Reclassification

The Company has reclassified its previously issued December 31, 2004 consolidated financial statements for certain operating expenses. This reclassification predominately related to certain store retail rents that were previously included in General and Administrative which have been reclassified to Selling. The reclassification had no effect on the consolidated balance sheet, the statement of stockholders equity or reported net income for the period.

The effect on the Company s previously issued 2004 financial statement is summarized as follows:

Statement of Income for the Year Ended December 31, 2004

	Previously Reported	Increase (Decrease)	As Reclassified
Selling	17,793,295	1,754,186	19,547,481
General and Administrative	15,820,631	(1,754,186)	14,066,445

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED INTERIM BALANCE SHEETS

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

	September 30, 2007	September 30, 2006
ASSETS		
Current		
Cash	$ 356,924	$ 223,223
Accounts receivable (Note 4)	1,762,506	2,049,173
Inventory	7,069,109	8,948,359
Advance U.S. affiliate (note 5)	1,144,020	
Current portion of deferred tax assets (Note 16)	168,000	141,000
Current portion of other assets	233,316	183,795
	10,733,875	11,545,550
Property and equipment (Note 6)	6,101,656	6,162,625
Deferred tax asset (Note 16)	387,000	260,000
Other Assets	277,622	270,850
	$ 17,500,153	$ 18,239,025
LIABILITIES		
Current		
Bank indebtedness (Note 7)	$ 885,000	$ 4,010,000
Accounts payable	1,343,803	1,223,968
Accounts payable U.S. affiliate (Note 15b)	487,405	351,219
Accrued liabilities	644,719	1,469,914
Accrued liabilities shareholder	2,646,212	1,824,400
Accrued payroll and vacation pay	595,377	526,659
Income tax payable	597,331	250,306
Demand loan (Note 8)	149,220	
Demand loan related party (Note 9)	994,800	
Current portion of deferred lease inducements	61,637	60,273
Current portion of capital lease obligations (Note 10)	13,481	46,850
Current portion of long-term debt (Note 11)	52,325	1,963,866
	8,471,310	11,727,455
Long-term debt (Note 11)	390,475	442,800
Deferred rent	877,771	613,711
Deferred lease inducements	81,237	141,510
Capital lease obligations (Note 10)		13,481

Long-term debt related parties (Note 12)	4,532,178	3,478,515
SHAREHOLDER S EQUITY		
Capital stock (Note 13)	2,010	1,710
Additional paid in capital	1,065,709	493,700
Retained earnings	2,079,463	1,326,143
	3,147,182	1,821,553
	$ 17,500,153	$ 18,239,025

See accompanying notes-

FS-79

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED INTERIM STATEMENTS OF ADDITIONAL PAID IN CAPITAL

AND RETAINED EARNINGS

FOR THE PERIODS ENDED SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

	Nine Months Ended	
	September 30, 2007	September 30, 2006
Additional Paid in Capital		
Balance, beginning of period	$ 580,444	$ 257,447
Imputed interest on shareholder loans (Note 12 b)	485,265	236,253
Balance, end of period	$ 1,065,709	$ 493,700
Retained Earnings		
Balance, beginning of period	$ 1,120,182	$ 1,208,974
Net income for the period	959,281	117,169
Balance, end of period	$ 2,079,463	$ 1,326,143

See accompanying notes

FS-80

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED INTERIM STATEMENTS OF OPERATIONS

FOR THE PERIODS ENDED SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

	Nine Months Ended	
	September 30, 2007	**September 30, 2006**
Sales	$ 33,100,119	$ 25,836,709
Cost of sales (including cost of sales attributed to purchases from the U.S. affiliate of $10,528,000 and $9,303,000 respectively)	(12,044,101)	(9,670,217)
Gross profit	21,056,018	16,166,492
Operating expenses		
Selling	10,004,052	8,853,800
Warehouse and distribution	2,488,115	2,143,039
General and administrative (including management fees charged by the shareholder of $3,000,000, and $1,824,400 respectively and consulting fees charged by an immediate family member of the shareholder of $172,475 and $139,040 respectively)	5,802,150	3,991,069
	18,294,317	14,987,908
Income before interest	2,761,701	1,178,584
Interest (including imputed interest on shareholder loans of $485,265 and $236,253 respectively, interest charged by family members of the shareholder and companies under their control of $207,497 and $149,230 respectively and interest earned from the U.S. affiliate of $110,491 and $Nil respectively)	(990,761)	(802,415)
Income before provision for income taxes	1,770,940	376,169
Provision for income taxes (Note 16)		
Current	894,659	413,000
Deferred	(83,000)	(154,000)
	811,659	259,000
Net income for the period	$ 959,281	$ 117,169

See accompanying notes

FS-81

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED INTERIM STATEMENTS OF CASH FLOWS (NOTE 17)

FOR THE PERIODS ENDED SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

	Nine Months Ended	
	September 30, 2007	**September 30, 2006**
Operating activities		
Net income for the period	$ 959,281	$ 117,169
Items not affecting cash:		
Depreciation and amortization	1,362,544	1,180,754
Loss on disposal of assets	46,100	
Amortization of deferred lease inducement	(43,840)	(45,204)
Imputed interest on shareholder loans	485,265	236,253
Deferred tax provision	(83,000)	(154,000)
Foreign exchange translation adjustment in investing activities	78,890	
Foreign exchange translation adjustment in financing activities	(573,677)	(134,569)
Deferred rent	105,941	208,269
	2,337,504	1,543,241
(Increase) decrease in accounts receivable	(445,870)	486,454
Decrease in accounts receivable U.S. affiliate	498,395	
Decrease (increase) in inventory	1,092,454	(1,555,104)
(Increase) decrease in other assets	(152,757)	14,878
Increase (decrease) in accounts payable	121,749	(1,009,104)
Increase (decrease) in accounts payable U.S. affiliate	487,405	(703,489)
Increase in accrued liabilities	290,979	762,139
Increase in accrued liabilities shareholder	1,513,055	124,400
Increase in accrued payroll and vacation pay	235,487	249,770
Decrease in income taxes payable	(17,382)	(64,346)
Lease inducement received		34,357
Cash provided by (used in) operating activities	5,961,019	(116,804)
Investing activities		
Additions to property and equipment	(894,741)	(937,248)
Advance U.S. affiliate	(1,222,910)	
Cash used in investing activities	(2,117,651)	(937,248)
Financing activities		
(Decrease) increase in bank indebtedness	(2,935,563)	464,356
Issuance of demand loan	159,810	
Issuance of demand loan related parties	1,225,210	
Repayment of capital lease obligations	(31,339)	(42,127)
Repayment of long-term debt	(1,507,362)	(485,528)
Issuance of long-term debt		353,216
Repayment of long-term debt related parties	(3,120,000)	(1,184,628)
Issuance of long-term debt related parties	2,222,500	1,926,480

Issuance of capital stock	300	
Cash (used in) provided by financing activities	(4,146,254)	1,031,769
Decrease in cash	(302,886)	(22,283)
Cash, beginning of period	659,810	245,506
Cash, end of period	$ 356,924	$ 223,223

See accompanying notes

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

NOTE 1 Basis of Presentation and Nature of Business

These combined financial statements include the accounts of the commonly owned companies American Apparel Canada Wholesale Inc. (formerly American Apparel Holdings Inc., 9072-1416 Quebec Inc. and 9001-9134 Quebec Inc.) and American Apparel Canada Retail Inc. (formerly the retail companies 9133-1090 Quebec Inc., 9137-4033 Quebec Inc., 9140-8880 Quebec Inc., 9154-1128 Quebec Inc., 9156-4526 Quebec Inc., 1614652 Ontario Ltd., 2061560 Ontario Ltd., 2061555 Ontario Ltd., 2061561 Ontario Ltd., 1646837 Ontario Ltd., 2083497 Ontario Inc., 2052199 Ontario Inc., 6294057 Canada Inc., 6294049 Canada Inc., 6338941 Canada Inc., 6362851 Canada Inc., 4300840 Canada Inc. and American Apparel Community Store and Gallery Inc.), herein referred to as The American Apparel Group of Canada. All significant intercompany accounts and transactions have been eliminated upon combining these entities.

These companies are incorporated under the Canada Business Corporations Act. American Apparel Canada Wholesale Inc. is engaged in the distribution of garments in Canada. American Apparel Canada Retail Inc. sells garments in Canada through retail outlets primarily under the name of American Apparel, herein referred to as the retail company.

On July 1, 2007, 9001-9134 Quebec Inc. and American Apparel Holdings Inc. were part of a reorganization with the parent of 9001-9134 Quebec Inc. (9072-1416 Quebec Inc.), effectively becoming one entity known as American Apparel Canada Wholesale Inc. On July 1, 2007, the retail companies were part of a reorganization, effectively becoming one entity known as American Apparel Canada Retail Inc.

On December 18, 2006, American Apparel, Inc. (U.S. affiliate) a company partially owned by the shareholder, together with the American Apparel Group of Canada (together referred to as American Apparel), entered into a definitive merger agreement with Endeavor Acquisition Corp. (Endeavour), a blank check company publicly traded on the American Stock Exchange. Upon consummation of the merger, Endeavor would acquire all of the outstanding capital stock of each of the Canadian companies of American Apparel and each would become a wholly-owned subsidiary of Endeavor. The merger is subject to customary closing conditions, and is expected to close in the second half of 2007. As part of the agreement, American Apparel is required to achieve certain financial targets. American Apparel is not in compliance with the financial targets. Endeavor has waived certain of these requirements. American Apparel and Endeavor can terminate the agreement at any time if mutually agreed. The agreement will terminate if a closing does not occur by December 15, 2007 and is subject to approval by the shareholders of Endeavor. There can be no assurance that the merger will be completed.

The financial information in this quarterly report reflects, in the opinion of management, all adjustments of a normal recurring nature necessary to present fairly the results for the interim period. Quarterly operating results are not necessarily indicative of the results that may be expected for other interim periods of the year ended December 31, 2007.

NOTE 2 Trade Name and Source of Supply

The companies existing business operating structure relies on the use of the trade name American Apparel and in sourcing principally all of their purchases from American Apparel, Inc. (Note 15 a) and b)).

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

NOTE 3 Summary of Significant Accounting Policies

The following is a summary of significant accounting policies followed in the preparation of the accompanying financial statements:

a) **Use of estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

b) **Cash**

The companies cash balances represent cash on deposit held at banks.

c) **Inventory valuation**

Inventory consists of finished goods and is valued at the lower of cost and net realizable value, determined on a first-in, first-out basis. Cost includes merchandise costs, duty and freight. Net realizable value is assessed using current demand information and historical experience. Inventory levels are reviewed in order to identify slow moving inventory and broken assortments, and markdowns are used to clear such inventory.

d) **Property and equipment**

Property and equipment are recorded at cost. Depreciation is provided for on a declining balance basis at rates designed to depreciate the cost of the property and equipment over their useful lives. The annual depreciation rates used are as follows:

Building	4%
Rolling stock	30%
Computer equipment and software	30%
Furniture and equipment	20%

Leasehold improvements are amortized on a straight-line basis over five years, which approximates the terms of the related lease.

e) **Impairment of long-lived assets**

The companies regularly review the carrying value of their long-lived assets. Whenever events or changes in circumstances indicate that the carrying amount of their assets might not be recoverable, the companies, using their best estimates based on reasonable and supportable assumptions and projections, adjust the carrying value of the related assets. Based upon the review of stores performances, no impairment charges were necessary.

f) **Deferred lease inducements**

Certain lease agreements provide for the companies to receive lease inducements from landlords to assist in the financing of certain property. Lease inducements are recorded as a deferred credit and amortized as a reduction of rent expense over the term of the related lease.

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

g) **Leased premises**

The companies record rent expense on a straight-line basis over the term of the lease. Accordingly, reasonably assured rent escalations and free-rent periods granted are deferred and amortized over the term of the lease. The difference between the recognized rent expense and amounts payable under the lease is recorded as a deferred rent liability. Operating expenses are recognized in the period in which the applicable costs are incurred. Percentage rents are recognized when the required level of sales has been achieved.

h) **Assets under capital lease**

Assets under capital lease are recorded at cost. The company provides for depreciation using the declining balance basis at rates designed to depreciate the cost of the assets under capital lease over their estimated useful lives. The annual depreciation rates used are as follows:

Computer equipment and software	30%
Furniture and equipment	20%

i) **Income taxes**

The companies follow the asset and liability method of accounting for income taxes. Under this method, income taxes must reflect the expected future tax consequences of temporary differences between the accounting basis of assets and liabilities and their tax basis. Deferred tax assets and liabilities are determined for each temporary difference based on the currently enacted tax rates expected to apply when the underlying income or expense items will be realized. A valuation allowance is recorded against any deferred tax asset if it is more likely than not the asset will not be realized. The effect of the changes in tax rates on deferred tax assets and liabilities is recognized in income in the period the changes occur.

j) **Revenue recognition**

Revenue from merchandise sales is net of returns and allowances, excluding sales taxes. The companies recognize product sales revenue when title and risk of loss have transferred to the customer, there is persuasive evidence of an arrangement, shipment and passage of title has occurred, the sales price is fixed or determinable and collectability is reasonably assured. Revenue from product sales are recorded at the time the product is shipped to the customer. With respect to their retail store operations, the companies recognize revenue upon the sale of their products to retail customers. The companies recognize the sales from gift cards, gift certificates and store credits as they are redeemed for merchandise. Prior to redemption, the companies maintain an unearned revenue liability for gift cards, gift certificates and store credits until the companies are released from such liability. The gift cards, gift certificates and store credits do not have expiration dates, and the companies maintain full liability and do not recognize any revenue from gift cards, gift certificates or store credits until redemption takes place.

k) **Sales returns and other allowances**

The companies analyze sales returns in accordance with Statement of Financial Accounting Standard (SFAS) No. 48 Revenue Recognition When Right of Return Exists (SFAS 48). The companies

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

are able to make reasonable and reliable estimates of product returns for their wholesale and retail store sales based on the companies past history. The companies also monitor the buying patterns of the end-users of their products based on sales data received by their retail outlets. Estimates for sales returns are based on a variety of factors including actual returns and based on expected return data communicated to them by customers. Accordingly, the companies believe that their historical returns analysis is an accurate basis for their allowance for sales returns. Actual results could differ from those estimates.

As with any set of assumptions and estimates, there is a range of reasonably likely amounts that may be calculated for each allowance above. However, the companies believe that there would be no significant difference in the amounts reported using other reasonable assumptions than what was used to arrive at each allowance. The companies regularly review the factors that influence their estimates and, if necessary, make adjustments when they believe that actual product returns, credits and other allowances may differ from established reserves. Actual experience associated with any of these items may be significantly different than the companies estimates.

l) **Cost of sales**

Cost of sales includes merchandise costs, duty and freight.

m) **Shipping and handling costs**

The companies incur shipping and handling costs in their operations. These costs consist of freight expenses incurred for third-party shippers to transport products to wholesale customers. They are included in Cost of Sales in the Combined Statements of Operations. Amounts billed to customers are included in Sales.

n) **Advertising costs**

Advertising and promotion costs are expensed as incurred.

o) **Store opening costs**

Expenditures associated with the opening of new stores, such as occupancy costs, payroll, advertising and promotion are expensed as incurred.

p) **Foreign currency translation**

Monetary assets and liabilities of the companies which are denominated in foreign currencies are translated at year end exchange rates. Other assets and liabilities are translated at rates in effect at the date the assets were acquired and liabilities incurred. Revenue and expenses are translated at the rates of exchange in effect at their transaction dates. The resulting gains or losses are included in operations.

q) **Accounting pronouncements newly issued**

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes-an Interpretation of FASB Statement No. 109 (the

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

Interpretation). The Interpretation establishes for all entities a minimum threshold for financial statement recognition of the benefit of tax positions, and requires certain expanded disclosures. The Interpretation is effective for fiscal years beginning after December 31, 2006, and is to be applied to all open tax years as of the date of effectiveness. The adoption of FASB Interpretation No. 48 did not have a material effect on the companies combined financial statements (Note 16).

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements , which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Adoption is required for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption of SFAS No. 157 is encouraged. The companies are currently evaluating the expected effect of SFAS No. 157 on their combined financial statements and are currently not yet in a position to determine such effects.

In September 2006, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108 (SAB 108) which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. SAB 108 is effective for fiscal years ending on or after November 15, 2006. The adoption of SAB 108 did not have a material impact on the companies combined financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption is required for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. The companies are currently evaluating the expected effect of SFAS No. 159 on their combined financial statements and are currently not yet in a position to determine such effects.

The FASB ratified the consensuses reached in Emerging Issues Task Force (EITF) Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation) (EITF 06-3). The EITF reached a consensus that the scope of the Issue includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, and may include, but is not limited to, sales, use, value added, and some excise taxes. The presentation of taxes within the scope of this Issue on either a gross or a net basis is an accounting policy decision that should be disclosed. Furthermore, for taxes reported on a gross basis, a company should disclose the aggregate amount of those taxes in interim and annual financial statements for each period for which an income statement is presented if that amount is significant. The disclosures required under this consensus should be applied retrospectively to interim and annual financial statements for all periods presented, if those amounts are significant. The companies have adopted EITF 06-3 on January 1, 2007. The adoption did not have a significant impact on their combined

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

financial position or results of operations. The companies record their sales net of any value added or sales tax.

All other recently issued accounting pronouncements are not expected to have material impact on the companies combined financial statements.

NOTE 4 Accounts Receivable

	September 30, 2007	September 30, 2006
Trade accounts receivable	$ 1,823,357	$ 2,103,645
Less:		
Allowance for doubtful accounts	(60,851)	(54,472)
	$ 1,762,506	$ 2,049,173

NOTE 5 Advance U.S. Affiliate

This advance to American Apparel Inc., of $1,150,000 U.S. bears interest at 18%, is due on demand and has no specific terms of repayment.

NOTE 6 Property and Equipment

	September 30, 2007		
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Building	$ 585,000	$ 64,652	$ 520,348
Furniture and equipment	1,315,151	534,991	780,160
Computer equipment and software	1,443,653	743,011	700,642
Leasehold improvements	7,277,085	3,252,770	4,024,315
Rolling stock	124,817	48,626	76,191
	$ 10,745,706	$ 4,644,050	$ 6,101,656

The above include assets under capital lease having an aggregate cost of $77,555 and an aggregate net book value of $33,640.

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

	September 30, 2006		
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Building	$ 585,000	$ 42,975	$ 542,025
Furniture and equipment	1,160,739	361,189	799,550
Computer equipment and software	1,227,930	493,014	734,916
Leasehold improvements	5,954,395	1,917,413	4,036,982
Rolling stock	76,217	27,065	49,152
	$ 9,004,281	$ 2,841,656	$ 6,162,625

The above include assets under capital lease having an aggregate cost of $177,555 and an aggregate net book value of $91,571.

NOTE 7 Bank Indebtedness

A company has a line of credit facility with maximum borrowings of $4,500,000, due on demand, bearing interest at the bank s prime rate (6.25% at September 30, 2007 and 6% at September 30, 2006) plus 1% per annum payable monthly. This line of credit is secured by a $5,000,000 moveable hypothec, which provides for a charge on the company s accounts receivable, inventory and all other moveable assets and by Section 427 Security under the Bank Act of Canada on inventory.

The bank s agreement contains various covenants which require the companies to maintain certain financial ratios and commitments as defined by the bank. As at September 30, 2007 and September 30, 2006, the company is not in compliance with one of these covenants. The bank has waived compliance with the obligation to meet this covenant as at September 30, 2007.

The shareholder has undertaken to subrogate an additional amount of approximately $1,410,500 U.S. in favor of the bank.

The retail company has provided unlimited corporate guarantees to secure this credit facility. These guarantees are secured by either moveable hypothecs in the amount of $3,200,000 or general assignment agreements. The shareholder has provided the bank with an unlimited guarantee. A member of the immediate family of the shareholder has provided the bank with a guarantee in the amount of $450,000 U.S.

NOTE 8 Demand Loan

This loan of $150,000 US from an employee of the U.S. affiliate, is due on demand, bears interest at 18% and has no specific terms of repayment.

NOTE 9 Demand Loan Related Party

This loan of $1,000,000 US from a company controlled by a relative of the shareholder, is due on demand, bears interest at 18% and has no specific terms of repayment.

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

NOTE 10 Capital Lease Obligations

	September 30, 2007	September 30, 2006
a) Lease, repayable in monthly installments of $3,446 including capital and interest at a rate of 14.59% per annum, repaid in the period (*secured by computer software having a net book value of approximately $46,000 as at September 30, 2006*).	$	$ 22,994
b) Leases, bearing interest at rates of approximately 15.27%, repayable in blended monthly payments aggregating $750, maturing in 2007, secured by furniture and equipment having a net book value of approximately $6,000 (*September 30, 2006 $11,000*).	553	8,654
c) Lease, repayable in monthly installments of $1,519 including capital and interest at a rate of 13.60% per annum, maturing in 2008, secured by furniture and equipment having a net book value of approximately $27,000 (*September 30, 2006 $34,000*).	12,928	28,683
	13,481	60,331
Deduct:		
Current portion	13,481	46,850
	$	$ 13,481

Total payments of obligations under capital lease are as follows:

	Capital	Interest	Total
2008	$ 13,481	$ 765	$ 14,246

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

NOTE 11 Long-Term Debt

	September 30, 2007	September 30, 2006
a) Various bank term loans, repayable in monthly capital installments aggregating $36,663 plus interest at rates ranging from the bank s prime rate (6.25% at September 30, 2007 and 6% at September 30, 2006) plus 2% to the bank s prime rate plus 3% per annum, maturing at dates ranging from 2008 to 2011. As a result of the reorganization of the retail companies as disclosed in Note 1, these loans were repaid in the period.	$	$ 1,437,990
b) Mortgage maturing November 2009, bearing interest at 4.85% per annum. The mortgage is secured by the building and is repayable in monthly installments of $2,462, combining principal and interest. An individual has provided the bank with a guarantee to secure this loan.	400,805	410,647
c) Loan from an individual, bearing interest at 14%, repayable in blended monthly payments of $21,366, maturing in 2007.	41,995	274,498
d) Loan from an individual, bearing interest at 6% per annum, repaid during 2006.		283,531
	442,800	2,406,666
Deduct:		
Current portion	52,325	1,963,866
	$ 390,475	$ 442,800

The bank term loans were secured by moveable hypothecs in the amount of $3,200,000 or general assignment agreements for certain of the retail companies.

9001-9134 Quebec Inc. had provided an unlimited guarantee of these term bank loans. These guarantees are secured by moveable hypothecs in the amount of $5,000,000.

Principal payments due in the next five years are as follows:

2008	$ 52,325
2009	10,843
2010	379,632
	$ 442,800

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

NOTE 12 Long-Term Debt Related Parties

	September 30, 2007	September 30, 2006
a) Loan of $450,000 U.S. (September 30, 2006 $450,000 U.S.) from a member of the immediate family of the shareholder, bearing interest at 18% and without terms of repayment. The loan has been subrogated in favour of the bank. This loan will not be repaid prior to October 1, 2008.	$ 447,660	$ 502,965
b) Loan from the shareholder, in the amount of $3,804,300 U.S. (September 30, 2006 $2,393,800 U.S.), non-interest bearing and without terms of repayment. An amount of $2,393,800 U.S. has been subrogated in favor of the bank, and the shareholder has undertaken to subrogate an additional $1,410,500 U.S. Interest of $485,265 (September 30, 2006 $236,253) has been imputed at an average interest rate of 14% (2006 14%), and has been credited as an addition to paid in capital. This loan will not be repaid prior to October 1, 2008.	3,784,518	2,675,550
c) Loan from a member of the immediate family of the shareholder, bearing interest at 18% and without terms of repayment. The loan has been subrogated in favour of the bank. This loan will not be repaid prior to October 1, 2008.	300,000	300,000
	4,532,178	3,478,515
Deduct:		
Current portion		
	$ 4,532,178	$ 3,478,515

NOTE 13 Capital Stock

Authorized

The following authorized classes of shares are unlimited in number and without par value:

American Apparel Canada Wholesale Inc. ***(formerly American Apparel Holdings Inc.)***

a) Class A Common shares

Voting, participating

b) Class B Common shares

Non-voting, participating

c) Class A Preferred shares

Voting, non-participating, non-cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

d) Class B Preferred shares
Non-voting, non-participating, non-cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

e) Class C Preferred shares
Voting, non-participating, non-cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

f) Class D Preferred shares
Non-voting, non-participating, non-cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

American Apparel Canada Retail Inc. ***(formerly the retail companies)***

a) Class A Common shares
Voting, participating

b) Class B Common shares
Non-voting, participating

c) Class A Preferred shares
Voting, non-participating, non-cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

d) Class B Preferred shares
Non-voting, non-participating, non-cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

e) Class C Preferred shares

Voting, non-participating, non-cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

f) Class D Preferred shares

Non-voting, non-participating, non-cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

9001-9134 Quebec Inc. ***(prior to the reorganization of July 1, 2007)***

a) Class A shares

Voting, participating

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

b) Class B shares
Non-voting, participating

c) Class C shares
Voting, at the rate of 100 votes per share, non-participating, retractable at an amount equal to the consideration for which such shares were issued

d) Class D shares
Non-voting, non-participating, non-cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

e) Class E shares
Non-voting, non-participating, non-cumulative monthly dividend of .75%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

f) Class F shares
Non-voting, non-participating, non-cumulative annual dividend based on the Bank of Canada prime rate, redeemable and retractable at an amount equal to the consideration for which such shares were issued

American Apparel Canada Wholesale Inc. has 33,153 Class A Common shares issued and outstanding for $210. American Apparel Canada Retail Inc. has 2,546 Class A Common shares issued and outstanding for $1,800.

As at September 30, 2006, 9001-9134 Quebec Inc. had 100 Class A shares issued and outstanding for $10. Each of the retail companies and American Apparel Holdings Inc. had 100 Class A Common shares issued and outstanding for $100 for an aggregate of 1,700 shares and $1,700.

NOTE 14 Commitments

The minimum rentals payable under long-term operating leases exclusive of certain operating costs for which the companies are responsible are approximately as follows:

2008	$ 3,492,000

2009	3,269,000
2010	3,018,000
2011	2,598,000
2012	2,624,000
Thereafter	7,102,000
	$ 22,103,000

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

Operating lease rent expense (including real estate taxes) was approximately $3,553,000 and $3,112,000 for the nine months ended September 30, 2007 and 2006 respectively. The companies did not incur any contingent rent during the periods. Rent expense is included in operating expenses. Certain lessors have registered security in support of the companies obligations.

NOTE 15 Related Party Transactions

a) The companies operate under the trade name American Apparel , the right of which belongs to American Apparel, Inc. Nominal fees are paid for the use of this name.

b) Purchases of approximately $9,249,000 U.S. and $9,233,000 U.S. ($9,765,000 CDN and $10,448,000 CDN) were made from American Apparel, Inc. for the nine months ended September 30, 2007 and 2006 respectively. The accounts payable U.S. affiliate of $489,953 U.S. (September 30, 2006 $304,832 US) relate to these purchases, are net of the charges described in Note 15 c) and are subject to normal trade terms.

c) A company paid expenses on behalf of American Apparel, Inc. in the amount of $1,915,857 and $836,482 for the nine months ended September 30, 2007 and 2006 respectively. These amounts have been applied against the accounts payable arising in Note 15 b).

d) The shareholder has provided a guarantee to the landlord of one of the companies. No fee has been paid for this guarantee.

These transactions are in the normal course of operations and were recorded at the exchange amount, which is the consideration established and agreed upon by the related parties.

NOTE 16 Income Taxes

On January 1, 2007, the company adopted the provisions of the Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB No. 109 (FIN No. 48). FIN No. 48 addresses the determination of how benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under FIN No. 48, the company must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate resolution. The companies did not recognize any additional liabilities for uncertain tax positions as a result of the implementation of FIN No. 48. The companies had no unrecognized tax benefits as of the date of adoption or as at September 30, 2007.

The companies uncertain tax positions are related to tax years that remain subject to examination by the relevant taxing authorities. The companies are currently open to audit for the fiscal years ended December 31, 2004 through September 30, 2007. The companies do not expect its unrecognized tax benefit position to change during the next twelve months. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position.

FS-95

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

The companies income tax provision has been determined as follows:

	Nine Months Ended	
	September 30, 2007	September 30, 2006
Net income before taxes for the period for accounting purposes	$ 1,770,940	$ 376,169
Temporary differences arising from:		
Depreciation and amortization	78,969	65,550
Eliminated intercompany profit on inventory	33,395	232,320
Deferred rent	105,941	208,269
Unrealized foreign exchange gain/loss	246,000	89,000
Permanent differences arising from:		
Non-deductible items	563,348	317,500
Net income for income tax purposes	$ 2,798,593	$ 1,288,808
Combined basic federal and provincial income tax at approximately 32%	$ 894,659	$ 413,000

The components of the deferred tax asset are as follows:

	September 30, 2007	September 30, 2006
Deferred tax asset arising from:		
Current		
Eliminated intercompany profit on inventory	$ 168,000	$ 141,000
Long-term		
Depreciation and amortization	$ 106,000	$ 64,000
Deferred rent	281,000	196,000
	$ 387,000	$ 260,000

NOTE 17 Supplemental Cash Flow Information

	Nine Months Ended	
	September 30, 2007	September 30, 2006
Cash paid for interest	$ 359,747	$ 513,083
Cash paid for income taxes	941,371	271,017

NOTE 18 Financial Instruments

a) **Credit risk**

The companies are not exposed in a material manner to credit risk from any individual customer. The companies review any new customer s credit history before extending credit and conduct regular reviews of their existing customers credit performance. Certain receivables have been insured. An allowance for doubtful accounts is established based upon factors relating to credit risk from specific customers, historical trends and other information.

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

b) **Forward contracts**

A company has purchased forward contracts for $2,500,000 U.S. which have a Canadian value of approximately $2,670,000 for future purchases denominated in U.S. dollars, which mature by December 2008. As at September 30, 2007, the unrealized loss with respect to these contracts amounts to approximately $183,000 CDN. This unrealized loss has been recorded in cost of sales and is included in accrued liabilities.

c) **Interest rate risk**

A company is exposed to interest rate fluctuations on its bank line of credit, as it bears interest at a rate of the bank s prime rate plus 1%.

d) **Fair value disclosure**

The carrying amount of accounts receivable, advance U.S. affiliate, bank indebtedness, accounts payable, accounts payable U.S. affiliate, accrued liabilities, accrued liabilities shareholder, accrued payroll and vacation pay, demand loan, demand loan related party, capital lease obligations, long-term debt and certain long-term debt related parties approximate their fair values.

The fair value of the long-term debt due to shareholder is less than carrying value, as the amount is non-interest bearing.

As the amount of long-term debt due to the shareholder and a member of the immediate family of the shareholder have no terms of repayment, the fair value cannot be calculated with any degree of certainty.

NOTE 19 Business Segment Information

The companies management reporting system evaluates performance based on a number of factors; however, the primary measures of performance are the net sales and income from operations of each segment, as these are the key performance indicator(s) reviewed by management. Operating income or loss for each segment does not include corporate general and administrative expenses and interest expense. Corporate general and administrative expenses include, but are not limited to: human resources, legal, finance, and various other corporate level activity related expenses. Such unallocated expenses remain within corporate. The accounting policies of all operating segments are the same as those described in the summary of significant accounting policies in Note 3.

The following table represents key financial information of the companies business segments:

	Nine Months Ended September 30, 2007		
	Wholesale	**Retail**	**Combined**
Net sales to external customers	$ 10,193,736	$ 22,906,383	$ 33,100,119
Income from operations	1,371,147	4,862,929	6,234,076
Depreciation and amortization	240,174	1,122,370	1,362,544
Capital expenditures	105,547	789,194	894,741
Deferred rent		105,941	105,941

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

NOTES TO THE COMBINED INTERIM FINANCIAL STATEMENTS (Continued)

AS AT SEPTEMBER 30, 2007 AND SEPTEMBER 30, 2006

(in Canadian dollars)

(unaudited)

	Nine Months Ended September 30, 2006		
	Wholesale	Retail	Combined
Net sales to external customers	$ 9,881,448	$ 15,955,261	$ 25,836,709
(Loss) income from operations	(991,971)	4,202,391	3,210,420
Depreciation and amortization	248,608	932,146	1,180,754
Capital expenditures	196,929	740,319	937,248
Deferred rent		208,269	208,269

Reconciliation to income before income taxes:

	Nine Months Ended	
	September 30, 2007	September 30, 2006
Combined income from operations of reportable segments	$ 6,234,076	$ 3,210,420
Corporate expenses	(3,472,375)	(2,031,836)
Interest expense	(990,761)	(802,415)
Combined income before income taxes	$ 1,770,940	$ 376,169

Identifiable assets by segment:

	September 30, 2007	September 30, 2006
Wholesale	$ 8,639,923	$ 9,215,640
Retail	8,860,230	9,023,385
	$ 17,500,153	$ 18,239,025

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholder of

The American Apparel Group of Canada

We have audited the accompanying combined balance sheets of **The American Apparel Group of Canada** as of December 31, 2006 and December 31, 2005 and the combined statements of retained earnings, operations and cash flows for the years then ended. These combined financial statements are the responsibility of the companies management. Our responsibility is to express an opinion on these combined financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether 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 control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the companies internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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 audit provides a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of **The American Apparel Group of Canada** as of December 31, 2006 and December 31, 2005 and the combined results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

CHARTERED ACCOUNTANTS

Montréal, Québec

August 8, 2007

(except for Note 3m) which is as at October 5, 2007)

Ce cabinet indépendant est exploité par

SNG Collins Barrow S.E.N.C.R.L./LLP.

Les marques de commerce de Collins

Barrow sont utilisées sous licence.

FS-99

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED BALANCE SHEETS

AS AT DECEMBER 31, 2006, 2005 AND 2004

(in Canadian dollars)

	2006	2005	2004 (unaudited)
ASSETS			
Current			
Cash	$ 659,810	$ 245,506	$
Accounts receivable (Note 4)	1,316,636	2,535,627	1,499,558
Accounts receivable U.S. affiliate (Note 12c)	498,395		
Income taxes recoverable			20,934
Inventory	8,161,563	7,393,255	5,447,319
Current portion of deferred tax asset (Note 13)	157,000	47,000	26,000
Current portion of other assets	153,638	287,351	374,357
	10,947,042	10,508,739	7,368,167
Property and equipment (Note 5)	6,615,560	6,406,131	3,641,853
Deferred tax asset (Note 13)	315,000	200,000	50,000
Other assets	204,543	182,172	87,739
	$ 18,082,145	$ 17,297,042	$ 11,147,759
LIABILITIES			
Current			
Bank indebtedness (Note 6)	$ 3,820,563	$ 3,545,644	$ 2,698,693
Accounts payable	1,222,054	2,233,072	554,287
Accounts payable U.S. affiliate (Note 12b)		1,054,708	1,797,995
Accrued liabilities	353,740	707,775	567,499
Accrued liabilities shareholder (Note 12d)	1,133,157	1,700,000	1,800,000
Accrued payroll and vacation pay	359,890	276,889	161,478
Income taxes payable	614,714	314,652	
Current portion of deferred lease inducements	60,272	53,157	
Current portion of capital lease obligations (Note 7)	36,057	57,638	52,630
Current portion of long-term debt (Note 8)	1,551,893	724,371	179,677
Current portion of long-term debt related parties (Note 9)		88,799	
	9,152,340	10,756,705	7,812,259
Deferred rent	771,830	405,442	77,307
Deferred lease inducements	126,442	159,472	
Capital lease obligations (Note 7)	8,763	44,820	99,762
Long-term debt (Note 8)	398,269	1,814,608	737,922
Long-term debt related parties (Note 9)	5,922,165	2,647,864	1,130,823

SHAREHOLDER S EQUITY			
Capital stock (Note 10)	1,710	1,710	910
Additional paid in capital	580,444	257,447	72,852
Retained earnings	1,120,182	1,208,974	1,215,924
	1,702,336	1,468,131	1,289,686
	$ 18,082,145	$ 17,297,042	$ 11,147,759

APPROVED:

See accompanying notes

FS-100

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED STATEMENTS OF ADDITIONAL PAID IN CAPITAL AND

RETAINED EARNINGS

FOR THE YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004

(in Canadian dollars)

	2006	2005	2004 (unaudited)
Additional Paid in Capital			
Balance, beginning of year	$ 257,447	$ 72,852	$
Imputed interest on shareholder loans (Note 9b)	322,997	184,595	72,852
Balance, end of year	$ 580,444	$ 257,447	$ 72,852
Retained Earnings			
Balance, beginning of year	$ 1,208,974	$ 1,215,924	$ 1,105,066
Net (loss) income for the year	(88,792)	(6,950)	110,858
Balance, end of year	$ 1,120,182	$ 1,208,974	$ 1,215,924

See accompanying notes

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED STATEMENTS OF OPERATIONS

FOR THE YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004

(in Canadian dollars)

	2006	2005	2004 (unaudited)
Sales	$ 34,657,769	$ 29,283,204	$ 17,378,646
Cost of sales (including cost of sales attributed to purchases from the U.S. affiliate of approximately $11,738,000; 2005 $10,454,000; 2004 $7,685,000)	12,851,745	11,465,815	8,786,194
Gross profit	21,806,024	17,817,389	8,592,452
Operating expenses			
Selling	11,848,397	9,819,414	3,260,455
Warehouse and distribution	3,446,312	2,439,095	1,276,373
General and administrative (including management fees charged by the shareholder of $2,320,000; 2005 $2,298,306; 2004 $1,813,908 and related party consulting fees of $101,429; 2005 $106,442; 2004 $88,174)	5,178,202	4,786,054	3,530,897
	20,472,911	17,044,563	8,067,725
Income before interest	1,333,113	772,826	524,727
Interest (including imputed interest on shareholder loans of $322,997; 2005 $184,595; 2004 $72,852 and related party interest of $186,000; 2005 $51,000; 2004 $51,000)	1,150,842	642,234	342,719
Income before provision for income taxes	182,271	130,592	182,008
Provision for income taxes (Note 13)			
Current	496,063	308,542	147,150
Deferred	(225,000)	(171,000)	(76,000)
	271,063	137,542	71,150
Net (loss) income for the year	$ (88,792)	$ (6,950)	$ 110,858

See accompanying notes

FS-102

Table of Contents

THE AMERICAN APPAREL GROUP OF CANADA

COMBINED STATEMENTS OF CASH FLOWS (NOTE 14)

FOR THE YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004

(in Canadian dollars)

	2006	2005	2004 (unaudited)
Operating activities			
Net loss for the year	$ (88,792)	$ (6,950)	$ 110,858
Items not affecting cash:			
Depreciation and amortization	1,671,451	1,146,287	378,429
Amortization of deferred lease inducement	(60,272)	(53,157)	
Imputed interest on shareholder loans	322,997	184,595	72,852
Deferred tax provision	(225,000)	(171,000)	(76,000)
Deferred rent	366,388	328,135	77,307
Gain on disposal of property and equipment		(2,752)	
	1,986,772	1,425,158	563,446
Decrease (increase) in accounts receivable	1,218,991	(1,036,069)	578,015
(Increase) in accounts receivable U.S. affiliate	(498,395)		
(Increase) in inventory	(768,308)	(1,945,936)	(2,062,163)
Decrease (increase) in income taxes recoverable		20,934	(20,934)
Decrease (increase) in other assets	111,342	(7,427)	(382,288)
(Decrease) increase in accounts payable	(1,011,018)	1,678,785	313,698
(Decrease) increase in accounts payable U.S. affiliate	(1,054,708)	(743,287)	1,200,053
(Decrease) increase in accrued liabilities	(354,035)	140,276	524,115
(Decrease) increase in accrued liabilities shareholder	(566,843)	(100,000)	1,037,658
Increase in accrued payroll and vacation pay	83,001	115,411	122,374
Increase (decrease) in income taxes payable	300,062	314,652	(259,021)
Lease inducements received	34,357	265,786	
Cash (used in) provided by operating activities	(518,782)	128,282	1,614,953
Investing activities			
Additions to property and equipment	(1,880,880)	(3,917,713)	(3,339,250)
Proceeds on disposal of property and equipment		9,900	
Cash used in investing activities	(1,880,880)	(3,907,813)	(3,339,250)
Financing activities			
Increase in bank indebtedness	274,919	846,951	249,015
Issuance of long-term debt	172,648	1,822,920	905,933
Repayment of long-term debt	(761,465)	(201,540)	(34,915)
Issuance of long-term debt related parties	4,107,561	1,605,840	628,527
Repayment of long-term debt related parties	(922,059)		
Repayment of capital lease obligations	(57,638)	(49,934)	(25,163)
Issuance of capital stock		800	900
Cash provided by financing activities	2,813,966	4,025,037	1,724,297
Increase in cash	414,304	245,506	

Cash, beginning of year	245,506		
Cash, end of year	$ 659,810	$ 245,506	$

See accompanying notes

FS-103

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 1 Basis of Presentation and Nature of Business

These combined financial statements include the accounts of the commonly owned companies 9001-9134 Quebec Inc., 9133-1090 Quebec Inc., 9137-4033 Quebec Inc., 9140-8880 Quebec Inc., 9154-1128 Quebec Inc., 9156-4526 Quebec Inc., 1614652 Ontario Ltd., 2061560 Ontario Ltd., 2061555 Ontario Ltd., 2061561 Ontario Ltd., 1646837 Ontario Ltd., 2083497 Ontario Inc., 6294057 Canada Inc., 6294049 Canada Inc., 6338941 Canada Inc., 6362851 Canada Inc., 4300840 Canada Inc. and American Apparel Holdings Inc., herein referred to as The American Apparel Group of Canada. All significant intercompany accounts and transactions have been eliminated upon combining these entities.

These companies are incorporated under the Canada Business Corporations Act except for 9001-9134 Quebec Inc., 9133-1090 Quebec Inc., 9137-4033 Quebec Inc., 9140-8880 Quebec Inc., 9154-1128 Quebec Inc., 9156-4526 Quebec Inc. which are incorporated under the laws of Quebec and 1614652 Ontario Ltd., 2061560 Ontario Ltd., 2061555 Ontario Ltd., 2061561 Ontario Ltd., 1646837 Ontario Ltd. and 2083497 Ontario Inc., which are incorporated under the laws of Ontario. These companies sell garments in Canada through retail outlets primarily under the name of American Apparel, herein referred to as the retail companies, other than 9001-9134 Quebec Inc., which is engaged in the distribution of garments. American Apparel Holdings Inc. owns a rental property occupied by the companies.

On July 1, 2007, the retail companies were part of a reorganization, effectively becoming one entity known as American Apparel Canada Retail Inc. On July 1, 2007, 9001-9134 Quebec Inc. and American Apparel Holdings Inc. were part of a reorganization with the parent of 9001-9134 Quebec Inc., effectively becoming one entity known as American Apparel Canada Wholesale Inc.

On December 18, 2006, American Apparel, Inc. (U.S affiliate) a company partially owned by the shareholder, together with the American Apparel Group of Canada (together referred to as American Apparel), entered into a definitive merger agreement with Endeavor Acquisition Corp. (Endeavor), a blank check company publicly traded on the American Stock Exchange. Upon consummation of the merger, Endeavor would acquire all of the outstanding capital stock of each of the Canadian companies of American Apparel and each would become a wholly-owned subsidiary of Endeavor. The merger is subject to customary closing conditions, and is expected to close in the second half of 2007. As part of the agreement, American Apparel is required to achieve certain financial targets. However, American Apparel is not in compliance with the financial targets. Endeavor has waived certain of these requirements. American Apparel and Endeavor can terminate the agreement at any time if mutually agreed. The agreement will terminate if a closing does not occur by December 15, 2007 and is subject to approval by the shareholders of Endeavor. There can be no assurance that the merger will be completed.

NOTE 2 Trade Name and Source of Supply

The companies existing business operating structure relies on the use of the trade name American Apparel and in sourcing principally all of its purchases from American Apparel, Inc. (Note 12 a) and b)).

As at December 31, 2006, American Apparel, Inc. has failed to meet certain debt covenants relating to its financing agreements with its bank and the current second lien lender. Subsequent to year-end, management has secured financing with a new bank and is in compliance with the covenants set forth in the new credit facility agreement.

FS-104

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 3 Summary of Significant Accounting Policies

The following is a summary of significant accounting policies followed in the preparation of the accompanying financial statements:

a) Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

b) Cash

The companies cash balances represent cash on deposit held at banks.

c) Inventory valuation

Inventory consists of finished goods and is valued at the lower of cost and net realizable value, determined on a first-in, first-out basis. Cost includes merchandise costs, duty and freight. Net realizable value is assessed using current demand information and historical experience. Inventory levels are reviewed in order to identify slow moving inventory and broken assortments, and markdowns are used to clear such inventory.

d) Property and equipment

Property and equipment are recorded at cost. Depreciation is provided for on a declining balance basis at rates designed to depreciate the cost of the property and equipment over their useful lives. The annual depreciation rates used are as follows:

Building	4%
Rolling stock	30%
Computer equipment and software	30%
Furniture and equipment	20%

Leasehold improvements are amortized on a straight line basis over five years, which approximates the terms of the related lease.

e) Impairment of long-lived assets

The companies regularly review the carrying value of their long-lived assets. Whenever events or changes in circumstances indicate that the carrying amount of their assets might not be recoverable, the companies, using their best estimates based on reasonable and supportable

assumptions and projections, adjust the carrying value of the related assets. Based upon the review of certain under-performing stores, a company has recorded impairment charges of $35,989 in 2006. These charges are included in depreciation and amortization.

f) Deferred lease inducements

Certain lease agreements provide for the companies to receive lease inducements from landlords to assist in the financing of certain property. Lease inducements are recorded as a deferred credit and amortized as a reduction of rent expense over the term of the related lease.

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

g) Leased premises

The companies record rent expense on a straight-line basis over the term of the lease. Accordingly, reasonably assured rent escalations and free-rent periods granted are deferred and amortized over the term of the lease. The difference between the recognized rent expense and amounts payable under the lease is recorded as a deferred rent liability. Operating expenses are recognized in the period in which the applicable costs are incurred. Percentage rents are recognized when the required level of sales has been achieved.

h) Assets under capital lease

Assets under capital lease are recorded at cost. The company provides for depreciation using the declining balance basis at rates designed to depreciate the cost of the assets under capital lease over their estimated useful lives. The annual depreciation rates used are as follows:

Computer equipment and software	30%
Furniture and equipment	20%

i) Income taxes

The companies follow the asset and liability method of accounting for income taxes. Under this method, income taxes must reflect the expected future tax consequences of temporary differences between the accounting basis of assets and liabilities and their tax basis. Deferred tax assets and liabilities are determined for each temporary difference based on the currently enacted tax rates expected to apply when the underlying income or expense items will be realized. A valuation allowance is recorded against any deferred tax asset if it is more likely than not the asset will not be realized. The effect of the changes in tax rates on deferred tax assets and liabilities is recognized in income in the year the changes occur.

j) Revenue recognition

Revenue from merchandise sales are net of returns and allowances, excluding sales taxes. The companies recognize product sales revenue when title and risk of loss have transferred to the customer, there is persuasive evidence of an arrangement, shipment and passage of title has occurred, the sales price is fixed or determinable and collectibility is reasonably assured. Revenue from product sales are recorded at the time the product is shipped to the customer. With respect to their retail store operations, the companies recognize revenue upon the sale of their products to retail customers. The companies recognize the sales from gift cards, gift certificates and store credits as they are redeemed for merchandise. Prior to redemption, the companies maintain an unearned revenue liability for gift cards, gift certificates and store credits until the companies are released from such liability. The gift cards, gift certificates and store credits do not have expiration dates, and the companies maintain full liability and do not recognize any revenue from gift cards, gift certificates or store credits until redemption takes place.

The company analyzes sales returns in accordance with Statement of Financial Accounting Standard (SFAS) No. 48 Revenue Recognition When Right of Return Exists (SFAS 48). The company is able to make reasonable and reliable estimates of product returns for its wholesale, on-line product

FS-106

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

sales and retail store sales based on the company s past history. The company also monitors the buying patterns of the end-users of its products based on sales data received by its retail outlets. Estimates for sales returns are based on a variety of factors including actual returns and based on expected return data communicated to it by customers. Accordingly, the company believes that its historical returns analysis is an accurate basis for its allowance for sales returns. Actual results could differ from those estimates.

k) Sales returns and other allowances

As with any set of assumptions and estimates, there is a range of reasonably likely amounts that may be calculated for each allowance above. However, the companies believe that there would be no significant difference in the amounts reported using other reasonable assumptions than what was used to arrive at each allowance. The companies regularly review the factors that influence their estimates and, if necessary, make adjustments when it believes that actual product returns, credits and other allowances may differ from established reserves. Actual experience associated with any of these items may be significantly different than the companies estimates.

l) Cost of sales

Cost of sales includes merchandise costs, duty and freight.

m) Shipping and handling costs

The companies incur shipping and handling costs in their operations. These costs consist of freight expenses incurred for third-party shippers to transport products to wholesale customers. Subsequent to the issuance of the Company s 2006 audited combined financial statements, in response to the SEC Observer statement in EITF 00-10, the Company has evaluated the significance of shipping and handling costs for the purpose of applying the guidance of this Issue based on the significance of those costs to each line item on the income statement that includes them and on their significance in total to gross margin. As a result of this analysis, the Company has decided to change its accounting method from classifying such costs in Selling to classifying them as part of Cost of Sales. In accordance with SFAS 154, retrospective application for this change in accounting principal was required and therefore the 2006 and prior period combined financial statements have been adjusted to reflect the reclassification of shipping and handling costs from Selling to Cost of Sales. The financial statement line items for Cost of Sales was increased and Selling was decreased by $324,109, $346,579 and $313,812 for the years ended December 31, 2006, 2005 and 2004, respectively. Shipping and handling costs included in Cost of Sales in the Combined Statements of Operations amounted to $324,109, $346,579 and $313,812 for the years ended December 31, 2006, 2005 and 2004, respectively. Amounts billed to customers of $324,326, $267,388 and $241,016 for the years ended December 31, 2006, 2005 and 2004, respectively are included in Sales.

n) Advertising costs

Advertising and promotion costs are expensed as incurred.

o) Store opening costs

Expenditures associated with the opening of new stores, such as occupancy costs, payroll, advertising and promotion are expensed as incurred.

FS-107

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

p) Foreign currency translation

Monetary assets and liabilities of the companies which are denominated in foreign currencies are translated at year end exchange rates. Other assets and liabilities are translated at rates in effect at the date the assets were acquired and liabilities incurred. Revenue and expenses are translated at the rates of exchange in effect at their transaction dates. The resulting gains or losses are included in operations.

q) Accounting Pronouncements Newly Issued

In May 2005, SFAS No. 154, Accounting Changes and Error Corrections replacement of APB Opinion No. 20 and FASB Statement No. 3, was issued. SFAS No. 154 changes the accounting for and reporting of a change in accounting principle by requiring retrospective application to prior periods financial statements of changes in accounting principle unless impracticable. SFAS No. 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 did not have a material impact on the Companies combined results of operations, financial position or cash flows.

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (the Interpretation). The Interpretation establishes for all entities a minimum threshold for financial statement recognition of the benefit of tax positions, and requires certain expanded disclosures. The Interpretation is effective for fiscal years beginning after December 31, 2006, and is to be applied to all open tax years as of the date of effectiveness. The Companies are in the process of evaluating the impact of the application of the Interpretation to their combined financial statements and are currently not yet in a position to determine such effects.

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements , which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Adoption is required for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption of SFAS No. 157 is encouraged. The Companies are currently evaluating the expected effect of SFAS No. 157 on their combined financial statements and are currently not yet in a position to determine such effects.

In September 2006, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 108 (SAB 108) which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. SAB 108 is effective for fiscal years ending on or after November 15, 2006. The adoption of SAB 108 did not have a material impact on the Companies combined financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS No. 159), which permits entities to choose to measure many financial instruments and certain other items at fair value. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption is required for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provision of SFAS No. 157. The Companies are currently evaluating

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

the expected effect of SFAS No. 159 in their combined financial statements and are currently not yet in a position to determine such effects.

The FASB ratified the consensuses reached in Emerging Issues Task Force (EITF) Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement (That Is, Gross versus Net Presentation) (EITF 06-3). The EITF reached a consensus that the scope of the Issue includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, and may include, but is not limited to, sales, use, value added, and some excise taxes. The presentation of taxes within the scope of this Issue on either a gross or a net basis is an accounting policy decision that should be disclosed. Furthermore, for taxes reported on a gross basis, a company should disclose the aggregate amount of those taxes in interim and annual financial statements for each period for which an income statement is presented if that amount is significant. The disclosures required under this consensus should be applied retrospectively to interim and annual financial statements for all periods presented, if those amounts are significant. The Companies will adopt EITF 06-3 on January 1, 2007. The Companies do not anticipate that the adoption will have a significant impact on their combined financial position or results of operations. The Companies currently records their sales net of any value added or sales tax.

All other recently issued accounting pronouncements are not expected to have a material impact on the Companies combined financial statements.

NOTE 4 Accounts Receivable

	2006	2005	2004 (unaudited)
Trade accounts receivable	$ 1,347,058	$ 2,567,248	$ 1,547,523
Less:			
Allowance for doubtful accounts	(30,422)	(31,621)	(47,965)
	$ 1,316,636	$ 2,535,627	$ 1,499,558

NOTE 5 Property and Equipment

		2006	
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Building	$ 585,000	$ 48,560	$ 536,440
Furniture and equipment	1,244,609	408,650	835,959
Computer equipment and software	1,348,921	571,807	777,114
Leasehold improvements	6,643,647	2,230,563	4,413,084
Rolling stock	85,217	32,254	52,963
	$ 9,907,394	$ 3,291,834	$ 6,615,560

The above include assets under capital lease having an aggregate cost of $177,555 and an aggregate net book value of $83,852.

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

		2005	
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Building	$ 585,000	$ 26,208	$ 558,792
Furniture and equipment	1,009,340	233,550	775,790
Computer equipment and software	1,072,969	304,848	768,121
Leasehold improvements	5,342,478	1,080,747	4,261,731
Rolling stock	57,246	15,549	41,697
	$ 8,067,033	$ 1,660,902	$ 6,406,131

The above include assets under capital lease having an aggregate cost of $177,555 and an aggregate net book value of $123,468.

		2004 (unaudited)	
	Cost	Accumulated Depreciation and Amortization	Net Book Value
Building	$ 585,000	$ 2,925	$ 582,075
Furniture and equipment	492,896	104,472	388,424
Computer equipment and software	465,366	121,419	343,947
Leasehold improvements	2,578,758	281,704	2,297,054
Rolling stock	51,815	21,462	30,353
	$ 4,173,835	$ 531,982	$ 3,641,853

NOTE 6 Bank Indebtedness

	2006	2005	2004 (unaudited)
Bank indebtedness arising from outstanding cheques	$ 485,563	$ 335,644	$ 288,693
Line of credit	3,335,000	3,210,000	2,410,000
	$ 3,820,563	$ 3,545,644	$ 2,698,693

A company has a line of credit facility with maximum borrowings of $4,500,000, due on demand, bearing interest at the bank s prime rate (6%, 5% and 4.25% at December 31, 2006, December 31, 2005 and December 31, 2004, respectively) plus 1% per annum payable monthly. This line of credit is secured by a $5,000,000 moveable hypothec, which provides for a charge on the company s accounts receivable, inventory and all

other moveable assets and by Section 427 Security under the Bank Act of Canada on inventory.

The bank s agreement contains various covenants which require the company to maintain certain financial ratios and commitments as defined by the bank. As at December 31, 2006 and December 31, 2005, the company was not in compliance with certain of these covenants. The bank has waived its right with respect to these

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

covenants as at December 31, 2006 and December 31, 2005. These covenants are measured quarterly. As at March 31, 2007 and March 31, 2006, the company was not in compliance with certain of these covenants. The bank has waived its right with respect to these covenants as at March 31, 2007 and March 31, 2006.

The shareholder has undertaken to subrogate an additional amount of approximately $1,508,000 in favor of the bank.

Certain of the companies have provided unlimited corporate guarantees to secure this credit facility. These guarantees are secured by either moveable hypothecs in the amount of $3,200,000 or general assignment agreements. The shareholder has provided the bank with an unlimited guarantee. A member of the immediate family of the shareholder has provided the bank with a guarantee in the amount of $450,000 U.S.

NOTE 7 Capital Lease Obligations

		2006	2005	2004 (unaudited)
a)	Lease, repayable in monthly installments of $3,446 including capital and interest at a rate of 14.59% per annum, maturing in 2007, secured by computer software having a net book value of approximately $39,000 (2005 $56,000; 2004 $80,000)	$ 13,377	$ 49,837	$ 81,377
b)	Leases, bearing interest at rates of approximately 15.27%, repayable in blended monthly payments aggregating $750 and maturing in 2007, secured by furniture and equipment having a net book value of approximately $15,000 (2005 $19,000; 2004 $24,000)	6,835	14,171	20,474
c)	Lease, repayable in monthly installments of $1,519 including capital and interest at a rate of 13.60% per annum, maturing in 2008, secured by furniture and equipment having a net book value of approximately $30,000 (2005 $38,000; 2004 $47,000)	24,608	38,450	50,541
		44,820	102,458	152,392
Deduct:				
	Current portion	36,057	57,638	52,630
		$ 8,763	$ 44,820	$ 99,762

Total payments of obligations under capital lease are as follows:

	Capital	Interest	Total
2007	$ 36,057	$ 3,269	$ 39,326
2008	8,763	351	9,114
	$ 44,820	$ 3,620	$ 48,440

FS-111

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 8 Long-Term Debt

		2006	2005	2004 (unaudited)
a)	Various bank term loans, repayable in monthly capital installments aggregating $36,663 plus interest at rates ranging from the bank s prime rate (6%, 5% and 4.25% at December 31, 2006, December 31, 2005 and December 31, 2004, respectively) plus 2% to the bank s prime rate plus 3% per annum, maturing at dates ranging from 2008 to 2011. As a result of the reorganization of the retail companies described in Note 1, these bank term loans were repaid subsequent to year end.	$ 1,322,561	$ 1,592,431	$ 490,833
b)	Mortgage maturing November 2009, bearing interest at 4.85% per annum. The mortgage is secured by the building and is repayable in monthly installments of $2,462, combining principal and interest. An individual has provided the bank with a guarantee to secure this loan.	408,231	417,723	426,766
c)	Loan from an individual, bearing interest at 14%, repayable in blended monthly payments of $21,366, maturing in 2007.	219,370	428,825	
d)	Loan from an individual, bearing interest at 6% per annum, repaid in the year.		100,000	
		1,950,162	2,538,979	917,599
Deduct:				
Current portion		1,551,893	724,371	179,677
		$ 398,269	$ 1,814,608	$ 737,922

The bank term loans are secured by moveable hypothecs in the amount of $3,200,000 or general assignment agreements for certain of the companies.

One of the companies has provided unlimited guarantees of these term bank loans. These guarantees are secured by moveable hypothecs in the amount of $5,000,000.

Principal payments due in the next five years are as follows:

2007	$ 1,551,893
2008	10,084
2009	10,584
2010	11,110
2011	11,663
Thereafter	354,828

	$ 1,950,162

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 9 Long-Term Debt Related Parties

		2006	2005	2004 (unaudited)
a)	Loan of $450,000 U.S. from a member of the immediate family of the shareholder, being a director of a company, bearing interest at 18% and without terms of repayment. The loan has been subrogated in favor of the bank. This loan will not be repaid prior to January 1, 2008.	$ 524,430	$ 523,350	$ 259,304
b)	Loans from the shareholder, including an amount of $2,393,800 U.S. ($2,789,735 CDN) (2005 $1,568,800 U.S.; $1,824,514 CDN; 2004 $560,000 U.S.; $812,552 CDN) non-interest bearing and without terms of repayment. An amount of $2,393,800 U.S. (2005 $1,568,800 U.S.; 2004 $560,000 U.S.) has been subrogated in favor of the bank, and the shareholder has undertaken to subrogate an additional $1,508,000 CDN. Interest of $322,997 (2005 $184,595; 2004 $72,852) has been imputed at an average interest rate of 14% (2005 14%; 2004 14%), and has been credited as an addition to paid in capital. These loans will not be repaid prior to January 1, 2008.	5,097,735	1,824,514	812,552
c)	Loan from a member of the immediate family of the shareholder, being a director of a company, bearing interest at 15% and without terms of repayment. The loan has been subrogated in favor of the bank. This loan will not be repaid prior to January 1, 2008.	300,000	300,000	
d)	Loan from a member of the immediate family of the shareholder, bearing interest at 12% per annum, repaid in the year.		88,799	58,967
		5,922,165	2,736,663	1,130,823
Deduct:				
Current portion			88,799	
		$ 5,922,165	$ 2,647,864	$ 1,130,823

NOTE 10 Capital Stock

Authorized

The following authorized classes of shares are unlimited in number and without par value:

9001-9134 Quebec Inc.

a) Class A shares
Voting, participating

FS-113

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

b) Class B shares
Non voting, participating

c) Class C shares
Voting, at the rate of 100 votes per share, non participating, retractable at an amount equal to the consideration for which such shares were issued

d) Class D shares
Non voting, non participating, non cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

e) Class E shares
Non voting, non participating, non cumulative monthly dividend of .75%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

f) Class F shares
Non voting, non participating, non cumulative annual dividend based on the Bank of Canada prime rate, redeemable and retractable at an amount equal to the consideration for which such shares were issued

Retail Companies

a) Class A Common shares
Voting, participating

b) Class B Common shares
Non voting, participating

c) Class A Preferred shares

Voting, non participating, non cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

d) Class B Preferred shares

Non voting, non participating, non cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

Retail Companies

e) Class C Preferred shares

Voting, non participating, non cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

f) Class D Preferred shares
Non voting, non participating, non cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

American Apparel Holdings Inc.

a) Class A Common shares
Voting, participating

b) Class B Common shares
Non voting, participating

c) Class A Preferred shares
Voting, non participating, non cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

d) Class B Preferred shares
Non voting, non participating, non cumulative monthly dividend of 1%, redeemable at an amount equal to the consideration for which such shares were issued

e) Class C Preferred shares
Voting, non participating, non cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

f) Class D Preferred shares
Non voting, non participating, non cumulative monthly dividend of 1%, redeemable and retractable at an amount equal to the consideration for which such shares were issued

As at December 31, 2006 and December 31, 2005, 9001-9134 Quebec Inc. has 100 Class A shares issued and outstanding for $10. As at December 31, 2006 and December 31, 2005, each of the retail companies and American Apparel Holdings Inc. has 100 Class A Common shares issued and outstanding for $100 for an aggregate of 1,700 shares and $1,700.

During 2005, 800 Class A shares of the retail companies were issued for $800.

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 11 Commitments

The minimum rentals payable under long term operating leases exclusive of certain operating costs for which the companies are responsible are approximately as follows:

2007	$ 3,457,000
2008	3,130,000
2009	2,916,000
2010	2,609,000
2011	2,105,000
Thereafter	7,532,000
	$ 21,749,000

Operating lease rent expense (including real estate taxes) was approximately $4,393,000 (2005 $3,222,000; 2004 $908,000). The companies did not incur any contingent rent during the year. Rent expense is included in operating expenses. Certain lessors have registered security in support of the companies obligations.

NOTE 12 Related Party Transactions

a) The companies operate under the trade name American Apparel , the right of which belongs to American Apparel, Inc. Nominal fees are paid for the use of this name.

b) Purchases of approximately $10,972,000 U.S. (2005 $10,309,000 U.S.; 2004 $7,497,000 U.S.) were made from American Apparel, Inc. The accounts payable U.S. affiliate of $Nil (2005 $907,000 U.S.; 2004 $1,496,000 U.S.) relate to these purchases and are subject to normal trade terms.

c) A company paid expenses on behalf of American Apparel, Inc. in the amount of $2,128,941 (2005 $1,520,023; 2004 $1,684,636). The accounts receivable U.S. affiliate ($427,660 U.S.; 2005 $Nil; 2004 $Nil) relate to these charges.

d) During the year, certain companies were charged management fees by the shareholder in the amount of $2,320,000 (2005 $2,298,306; 2004 $1,813,908). The accrued liabilities shareholder relate to these charges.

e) During the year, a company paid consulting fees to an immediate family member of the shareholder, being a director, in the amount of $101,429 (2005 $106,442; 2004 $88,174).

f) During the year, a company paid interest to an immediate family member of the shareholder, being a director, in the amount of approximately $169,000 (2005 $42,000; 2004 $51,000) and a second immediate family member of the shareholder in the amount of approximately $17,000 (2005 $9,000; 2004 $Nil).

g) The shareholder has provided a guarantee to the landlord of one of the companies. No fee has been paid for this guarantee.

These transactions are in the normal course of operations and were recorded at the exchange amount, which is the consideration established and agreed upon by the related parties.

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 13 Income Taxes

The companies income tax provision has been determined as follows:

	2006	2005	2004 (unaudited)
Net income for the year for accounting purposes	$ 182,271	$ 130,592	$ 182,008
Temporary differences arising from:			
Depreciation and amortization	64,000	165,000	10,000
Eliminated intercompany profit on inventory	342,662	64,537	83,644
Deferred rent	366,388	328,135	
Permanent differences arising from:			
Non-deductible items	587,499	281,633	187,632
Net Income for Income Tax Purposes	$ 1,542,820	$ 969,897	$ 463,284
Combined Basic Federal and Provincial Income Tax at Approximately 32%	$ 496,063	$ 308,542	$ 147,150

The components of the deferred tax asset are as follows:

	2006	2005	2004 (unaudited)
Deferred tax asset arising from:			
Current			
Eliminated intercompany profit on inventory	$ 157,000	$ 47,000	$ 26,000
Long-Term			
Depreciation and amortization	$ 70,000	$ 60,000	$ 25,000
Deferred rent	245,000	140,000	25,000
	$ 315,000	$ 200,000	$ 50,000

NOTE 14 Supplemental Cash Flow Information

	2006	2005	2004 (unaudited)
a) **Cash Flow Information:**			
Cash paid for interest	$ 689,489	$ 356,280	$ 216,043

Cash paid for (net of recoveries from) income taxes	196,001	(28,364)	299,401
b) **Non-Cash Financing and Investing:**			
Assets acquired under capital leases	$	$	$ 177,555

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 15 Financial Instruments

a) **Credit risk**

The companies are not exposed in a material manner to credit risk from any individual customer. The companies review any new customer s credit history before extending credit and conduct regular reviews of their existing customers credit performance. Certain receivables have been insured. An allowance for doubtful accounts is established based upon factors relating to credit risk from specific customers, historical trends and other information.

b) **Forward contracts**

A company has purchased forward contracts for $1,150,000 U.S. which have a Canadian value of approximately $1,277,000 for future purchases denominated in U.S. dollars, which mature by November 2007. As at December 31, 2006, the unrealized gain with respect to these contracts amounts to approximately $63,000 CDN. This unrealized gain has been recorded in cost of sales and is included in other assets.

c) **Interest rate risk**

Certain companies are exposed to interest rate fluctuations on their bank line of credit and bank loans, as they bear interest at rates ranging from the bank s prime rate plus 1% to the bank s prime rate plus 3%.

d) **Fair value disclosure**

The carrying amount of accounts receivable, accounts receivable U.S. affiliate, bank indebtedness, accounts payable, accounts payable U.S. affiliate, accrued liabilities, accrued liabilities shareholder, accrued payroll and vacation pay, capital lease obligations long-term debt and certain long-term debt related parties approximate their fair values.

The fair value of the long-term debt due to shareholder is less than carrying value, as the amount is non-interest bearing.

As the amount of long-term debt due to the shareholder and a member of the immediate family of the shareholder have no terms of repayment, the fair value cannot be calculated with any degree of certainty.

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

NOTE 16 Business Segment Information

The companies management reporting system evaluates performance based on a number of factors; however, the primary measures of performance are the net sales and income from operations of each segment, as these are the key performance indicators reviewed by management. Operating income or loss for each segment does not include corporate general and administrative expenses and interest expense. Corporate general and administrative expenses include, but are not limited to: human resources, legal, finance and various other corporate level activity related expenses. Such unallocated expenses remain within corporate. The accounting policies of all operating segments are the same as those described in the summary of significant accounting policies in Note 3.

The following table represents key financial information of the companies business segments:

		2006	
	Wholesale	Retail	Combined
Net sales to external customers	$ 12,643,985	$ 22,013,784	$ 34,657,769
Income from operations	584,013	3,321,108	3,905,121
Depreciation and amortization	314,944	1,296,235	1,611,179
Capital expenditures	239,276	1,641,604	1,880,880
Deferred rent		366,388	366,388

		2005	
	Wholesale	Retail	Combined
Net sales to external customers	$ 13,686,933	$ 15,596,271	$ 29,283,204
Income from operations	1,081,176	2,359,800	3,440,976
Depreciation and amortization	271,866	821,264	1,093,130
Capital expenditures	476,672	3,441,041	3,917,713
Deferred rent		328,135	328,135

		2004 (unaudited)	
	Wholesale	Retail	Combined
Net sales to external customers	13,374,352	4,004,294	17,378,646
Income from operations	2,267,102	340,639	2,607,741
Depreciation and amortization	181,367	197,062	378,429
Capital expenditures	1,087,324	2,429,481	3,516,805
Deferred rent		77,307	77,307

Reconciliation to income before income taxes:

	2006	2005	2004

			(unaudited)
Combined income from operations of reportable segments	$ 3,905,121	$ 3,440,976	$ 2,607,741
Corporate expenses	(2,572,008)	(2,668,150)	(2,083,014)
Interest expense	(1,150,842)	(642,234)	(342,719)
Combined income before income taxes	$ 182,271	$ 130,592	$ 182,008

FS-119

Table of Contents

The American Apparel Group of Canada

Notes to Combined Financial Statements (Continued)

(in Canadian dollars)

As At December 31, 2006, 2005 and 2004

Identifiable assets by segment:

	2006	2005	2004 (unaudited)
Wholesale	$ 8,481,471	$ 8,651,391	$ 6,705,288
Retail	9,600,674	8,645,651	4,442,471
Total	$ 18,082,145	$ 17,297,042	$ 11,147,759

FS-120

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Condensed Balance Sheets

	September 30, 2007 (unaudited)	December 31, 2006
Assets		
Current assets:		
Cash	$ 101,007	$ 166,527
Cash held in Trust Fund	128,374,498	125,113,007
Prepaid expenses and other current assets	28,476	116,738
Total current assets	128,503,981	125,396,272
Deferred acquisition costs	431,314	145,808
Equipment, net of accumulated depreciation $1,767 and $631, respectively	2,777	3,914
Total assets	$ 128,938,072	$ 125,545,994
Liabilities and Stockholders Equity		
Current liabilities:		
Accrued expenses	$ 599,241	$ 260,076
Notes payable related party	475,000	
Total current liabilities	1,074,241	260,076
Common Stock, subject to possible conversion, 3,232,148 shares at conversion value	25,673,970	25,021,696
Commitment and Contingencies		
Stockholders Equity		
Preferred stock, $.0001 par value, authorized 1,000,000 shares; none issued		
Common stock, $.0001 par value, authorized 75,000,000 shares, issued and outstanding 19,910,745 shares (less 3,232,148 subject to possible conversion)	1,668	1,668
Additional paid-in capital	96,685,829	97,338,103
Earnings accumulated during development stage	5,502,364	2,924,451
Total stockholders equity	102,189,861	100,264,222
Total liabilities and stockholders equity	$ 128,938,072	$ 125,545,994

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

FS-121

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Condensed Statements of Operations

(unaudited)

For the Three and Nine Months Ended September 30, 2007 and 2006,

And the period July 22, 2005 (inception) to September 30, 2007

	For the three months ended September 30, 2007	For the three months ended September 30, 2006	For the nine months ended September 30, 2007	For the nine months ended September 30, 2006	For the period July 22, 2005 (inception) to September 30, 2007
Revenue	$	$	$	$	$
General, selling and administrative expenses	172,404	286,512	686,325	705,560	1,854,086
Operating Loss	(172,404)	(286,512)	(686,325)	(705,560)	(1,854,086)
Dividend and interest income	1,112,492	1,031,673	3,264,238	2,897,916	7,356,450
Income before provision for income taxes	940,088	745,161	2,577,913	2,192,356	5,502,364
Benefit for income taxes		252,148			
Net income	940,088	997,309	2,577,913	2,192,356	5,502,364
Accretion of Trust Fund relating to Common Stock subject to possible conversion	(222,490)	(205,725)	(652,274)	(579,786)	(1,469,614)
Net income attributable to common stockholders	$ 717,598	$ 791,584	$ 1,925,639	$ 1,612,570	$ 4,032,750
Weighted average basic shares outstanding	16,678,713	16,678,713	16,678,713	16,668,470	
Weighted average diluted shares outstanding	16,739,305	16,678,713	16,748,738	16,668,470	
Basic income per share	$ .04	$ .05	$ .12	$ .10	
Diluted income per share	$ .04	$ .05	$ .11	$ .10	

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

Endeavor Acquisition Corp.

(a development stage enterprise)

Condensed Statement of Stockholders Equity

(unaudited)

For the Nine Months Ended September 30, 2007

	Common Stock			Earnings accumulated during development stage	Total stockholders equity
	Shares	Amount	Additional paid-in capital		
Balance, January 1, 2007	19,910,745	$ 1,668	$ 97,338,103	$ 2,924,451	$ 100,264,222
Accretion of Trust Fund relating to Common Stock subject to possible conversion			(652,274)		(652,274)
Net income for the nine months ended September 30, 2007				2,577,913	2,577,913
Balance, September 30, 2007	19,910,745	$ 1,668	$ 96,685,829	$ 5,502,364	$ 102,189,861

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

FS-123

Endeavor Acquisition Corp.

(a development stage enterprise)

Condensed Statements of Cash Flows

(unaudited)

For the Nine Months Ended September 30, 2007 and 2006 and

For the Period July 22, 2005 (inception) to September 30, 2007

	For the Nine months ended September 30, 2007	For the Nine months ended September 30, 2006	For the period July 22, 2005 (inception) to September 30, 2007
Cash Flows from Operating Activities			
Net income	$ 2,577,913	$ 2,192,356	$ 5,502,364
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	1,137	252	1,767
Changes in operating assets and liabilities:			
Decrease (increase) in prepaid expenses and other current assets	88,262	120,922	(28,476)
Increase in accrued expenses	53,659	148,778	167,927
Net cash provided by operating activities	2,720,971	2,462,308	5,643,582
Cash Flows from Investing Activities			
Cash held in Trust Fund	(3,261,491)	(11,735,137)	(128,374,498)
Purchase of equipment		(4,545)	(4,545)
Net cash used in investing activities	(3,261,491)	(11,739,682)	(128,379,043)
Cash Flows from Financing Activities			
Proceeds from sale of stock to initial stockholders			25,000
Gross proceeds from initial public offering			120,000,000
Gross proceeds from overallotment option		9,285,860	9,285,860
Proceeds from issuance of option			100
Payment of offering costs		(445,727)	(6,949,492)
Proceeds from issuance of notes payable related party	475,000		475,000
Net cash provided by financing activities	475,000	8,840,133	122,836,468
Net (decrease) increase in cash	(65,520)	(437,241)	101,007
Cash at beginning of the period	166,527	1,144,634	
Cash at end of the period	$ 101,007	$ 707,393	$ 101,007
Supplemental Disclosures of Noncash Transactions:			
Accrual of deferred acquisition costs:			
Deferred acquisition costs	$ 285,506	$	$ 431,314
Accrued expenses payable	(285,506)		(431,314)

	$	$	$

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

FS-124

Table of Contents

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

1. Interim Financial Information

Endeavor Acquisition Corp. s (the Company) unaudited condensed interim financial statements as of September 30, 2007 and for the three and nine months ended September 30, 2007 and 2006, and for the period July 22, 2005 (inception) to September 30, 2007 have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In addition, the December 31, 2006 balance sheet data was derived from the audited financial statements, but does not include all disclosures required by GAAP. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the interim period presented are not necessarily indicative of the results to be expected for any other interim period or for the full year.

These unaudited condensed interim financial statements should be read in conjunction with the audited financial statements and notes thereto for the fiscal year ended December 31, 2006 included in the Company s Form 10-K for the fiscal year ended December 31, 2006, filed on March 16, 2007. The accounting policies used in preparing these unaudited condensed financial statements are consistent with those described in the December 31, 2006 audited financial statements except for the adoption of FIN 48 which is discussed in Note 9.

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

2. Organization and Business Operations

The Company was incorporated in Delaware on July 22, 2005 as a blank check company, whose objective is to acquire an operating business.

All activity from July 22, 2005 through December 21, 2005 related to the Company s formation and initial public offering as described below. Since December 22, 2005, the Company has been searching for a target business to acquire. The Company has selected December 31 as its fiscal year end.

The Company s management has broad discretion with respect to the specific application of the net proceeds of this Offering, although substantially all of the net proceeds of this Offering are intended to be generally

applied toward consummating a business combination with an operating business (Business Combination   ). Furthermore, there is no assurance that the Company will be able to successfully effect a Business Combination. An amount of $121,030,234 of the net proceeds from the initial public offering and the exercise of the underwriters   overallotment

Table of Contents

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS (Continued)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

option was deposited and is being held in an interest-bearing trust account (Trust Account) until the earlier of (i) the consummation of a Business Combination or (ii) liquidation of the Company. As of September 30, 2007, the balance in the Trust Account was $128,374,498, which includes $7,344,264 of cumulative interest and dividends earned since inception of the Trust Account. Under the agreement governing the Trust Account, funds will only be invested in United States government securities within the meaning of Section 2(a)(16) of the Investment Company Act of 1940, having a maturity of 180 days or less, or in money market funds meeting certain conditions under Rule 2a-7 promulgated under the Investment Company Act of 1940. The remaining net proceeds (not held in the Trust Account) may be used to pay for business, legal and accounting due diligence on prospective acquisitions and continuing general and administrative expenses.

The Company, after signing a definitive agreement for the acquisition of a target business, will submit such transaction for stockholder approval. In the event that stockholders owning 20% or more of the shares sold in the Offering vote against the Business Combination and exercise their conversion rights described below, the Business Combination will not be consummated.

All of the Company s stockholders prior to the Offering, including all of the officers and directors of the Company (Initial Stockholders), have agreed to vote their 3,750,000 founding shares of common stock in accordance with the vote of the majority in interest of all other stockholders of the Company (Public Stockholders) with respect to any Business Combination. After consummation of a Business Combination, these voting safeguards will no longer be applicable.

With respect to a Business Combination which is approved and consummated, any Public Stockholder who voted against the Business Combination may demand that the Company convert their shares. The per share conversion price will equal the amount in the Trust Account, calculated as of two business days prior to the consummation of the proposed Business Combination, divided by the number of shares of common stock held by Public Stockholders at the consummation of the Offering. Accordingly, Public Stockholders holding 20% (less one share) of the aggregate number of shares owned by all Public Stockholders may seek conversion of their shares in the event of a Business Combination. Such Public Stockholders are entitled to receive their per share interest in the Trust Account computed without regard to the shares held by Initial Stockholders. Accordingly, a portion of the net proceeds from the offering (20% (less one share value) of the amount held in the Trust Account) amounting to $25,673,970 has been classified as common stock subject to possible conversion in the accompanying September 30, 2007 unaudited condensed balance sheet.

The Company s Certificate of Incorporation provides for mandatory liquidation of the Company in the event that the Company does not consummate a Business Combination within 18 months from the date of the consummation of the Offering (July 21, 2007), or 24 months from the consummation of the Offering (December 21,

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS (Continued)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

2007) if certain extension criteria have been satisfied. The extension criteria was satisfied by filing a definitive agreement stating that the Company intends to acquire American Apparel, Inc. and its affiliated companies (collectively American Apparel) in an 8K filed with the SEC on December 20, 2006. In the event of liquidation, it is likely that the per share value of the residual assets remaining available for distribution (including Trust Account assets) will be less than the initial public offering price per share in the Offering due to costs related to the Offering and since no value would be attributed to the Warrants contained in the Units sold.

Management does not believe that any recently issued, but not yet effective, accounting standards if currently adopted would have a material effect on the accompanying unaudited interim condensed financial statements.

3. Going Concern and Management Plans

As of September 30, 2007, the Company has negative working capital of $944,758, net of $128,374,498 of which is cash held in the Trust Account. On December 18, 2006, the Company entered into an agreement to acquire an operating entity expected to be consummated in 2007. In order for the Company to continue to fund the operating costs associated with the acquisition, the Company s officers have agreed to advance the Company enough capital in order to consummate the acquisition. There can be no assurance that the acquisition will be consummated. Should this Business Combination not be consummated, the Company would be required to return the funds held in the Trust Account to holders of shares issued in the Offering, as a mandatory liquidation, pursuant to a plan of dissolution and liquidation approved by stockholders. These conditions raise substantial doubt about the Company s ability to continue as a going concern. The unaudited condensed interim financial statements do not include any adjustments that might result from the outcome of this uncertainty.

4. Notes Payable - Related Party

On March 8, 2007, the Company borrowed funds from two of the Company s officers. The Company issued two promissory notes in the amount of $75,000 each. The principal balance of these notes shall be repayable on the earlier of the consummation of the Company s business combination with American Apparel or upon demand by the officers. These promissory notes are noninterest bearing.

On April 30, 2007, the Company borrowed funds from two of the Company s officers. The Company issued two promissory notes in the amount of $87,500 each. The principal balance of these notes shall be repayable on the earlier of the consummation of the Company s business combination with American Apparel or upon demand by the officers. These promissory notes are non-interest bearing.

On August 31, 2007, the Company borrowed funds from two of the Company s officers. The Company issued two promissory notes in the amount of $75,000 each. The principal balance of these notes shall be repayable on the earlier of the consummation of the Company s business combination with American Apparel or upon demand by the officers. These promissory notes are non-interest bearing.

Table of Contents

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS (Continued)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

5. Earnings Per Share

Basic earnings per share (EPS) is computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is calculated by dividing net income available to common stockholders by the weighted-average number of shares of common stock and the dilutive effect of outstanding Units as if exercised. Common shares subject to possible conversion of 3,232,148 have been excluded from the calculation of basic earnings per share since such shares, if redeemed, only participate in their pro-rata shares of the trust earnings. The September 30, 2006 earnings per share presentation for the three and nine months ended September 30, 2006 was revised to conform with this policy and to the current three and nine months presentation. The conversion of the outstanding warrants, totaling 16,160,745, is contingent upon the occurrence of future events, and therefore, is not includable in the calculation of diluted earnings per share in accordance with Statement of Financial Accounting Standards (SFAS) No. 128, Earnings per Share. The following is a reconciliation between basic and diluted EPS:

	Three Months Ended		Nine Months Ended	
	September 30, 2007	September 30, 2006	September 30, 2007	September 30, 2006
Numerator:				
Numerator for basic and diluted EPS net income attributable to common stockholders	$ 717,598	791,584	1,925,639	1,612,570
Denominator:				
Denominator for basic EPS weighted average shares outstanding	16,678,713	16,678,713	16,678,713	16,668,470
Effect of dilutive units	60,592		70,025	
Denominator for dilutive EPS weighted average shares	16,739,305	16,678,713	16,748,738	16,668,470
Basic EPS	$ .04	$ .05	$ .12	$ .10
Diluted EPS	$ .04	$ .05	$ .11	$ .10

6. Commitment and Contingencies

The Company has previously been incurring a fee from Ironbound Partners Fund LLC, an affiliate of Jonathan J. Ledecky, our president and secretary, of $7,500 per month for providing the Company with office space and certain general and administrative services. This relationship has been terminated as of January 1, 2007. The Company entered into a month to month lease agreement with an unaffiliated party for the period January 1, 2007 through April 30, 2007. The Company subsequently paid rent expense from May 1, 2007 to September 30, 2007 as needed. During the three and nine months ended September 30, 2007 the Company incurred $0 and $12,000 rent expense, respectively. As of November 1, 2007 the Company

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS (Continued)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

will lease office space for the benefit of their consultants from an unaffiliated party at the cost of $2,500 per month.

Pursuant to letter agreements with the Company and Ladenburg Thalmann & Co. Inc., the representative of the underwriters in the Offering (Representative), the

Initial Stockholders have waived their rights to receive distributions with respect to their founding shares upon the Company s liquidation.

The Initial Stockholders are entitled to registration rights with respect to their founding shares pursuant to an agreement dated December 15, 2005. The holders of the majority of these shares are entitled to make up to two demands that the Company register these shares at any time commencing three months prior to the third anniversary of the effective date of the Offering. In addition, the Initial Stockholders have certain piggy-back registration rights on registration statements filed subsequent to the third anniversary of the effective date of the Offering.

The Representative has agreed to defer a portion of its underwriting commission earned upon consummation of the Offering. The deferred commission, totaling $1.825 million will not be payable unless and until the Company completes a Business Combination. Additionally, the Representative has waived their right to receive such payment upon the Company s liquidation if it is unable to complete a Business Combination. Accordingly, the deferred commission will be charged to stockholders equity upon the completion of a Business Combination.

The Company entered into a consulting agreement with a consultant on July 17, 2006 to perform services through December 15, 2007. The Company pays the consultant a fee of $125,000 per year and the Company will issue to the consultant 12,500 shares of the Company s common stock upon the closing of the initial business combination by the Company. The Company will also issue to the consultant an additional 12,500 shares of the Company s common stock six months after closing of the initial business combination by the Company.

In December 2006, the Company retained the services of ICR, LLC (ICR) as an investor relations consultant to assist the Company in developing and disseminating investor presentations and communications. the Company pays ICR a fee of $12,000 per month, plus expenses, and will issue ICR 9,700 shares of the Company s common stock upon consummation of the pending acquisition (see Note 8).

7. Initial Public Offering

On December 21, 2005, the Company sold 15,000,000 units (Units) in the Offering at $8.00 per Unit. On January 5, 2006, the Company sold an additional 1,160,745 Units pursuant to the underwriters over-allotment option. Each Unit consists of one share of the Company s common stock, $.0001 par value, and one Redeemable Common Stock Purchase Warrant (Warrants). Each Warrant entitles the holder to purchase from the Company one share of common stock at an exercise price of $6.00 commencing the later of the completion of a Business Combination or

Table of Contents

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS (Continued)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

December 15, 2006 and expiring on December 14, 2009. The Warrants will be redeemable by the Company, at a price of $.01 per Warrant upon 30 days notice after the Warrants become exercisable, only in the event that the last sale price of the common stock is at least $11.50 per share for any 20 trading days within a 30 trading day period ending on the third day prior to the date on which notice of redemption is given. There is no cash settlement option for the Warrants. In connection with this Offering, the Company issued an option, for $100, to the Representative to purchase 350,000 Units at an exercise price of $10.00 per Unit.

The Company has accounted for the fair value of the option, inclusive of the receipt of the $100 cash payment, as an expense of the public offering resulting in a charge directly to stockholders equity. The Company estimated that the fair value of this option is approximately $703,500 ($2.01 per Unit) using a Black-Scholes option-pricing model. The fair value of the option granted to the Representative is estimated as of the date of grant using the following assumptions: (1) expected volatility of 52.7%, (2) risk-free interest rate of 4.43%, (3) expected life of two years and 30 days and (4) dividend rate of zero. The option may be exercised for cash or on a cashless basis at the holder s option, such that the holder may use the appreciated value of the option (the difference between the exercise prices of the option and the underlying Warrants and the market price of the Units and underlying securities) to exercise the option without the payment of any cash. There is no cash settlement option for the underwriters purchase options, or for the Warrants contained in the units to be purchased by the underwriters.

8. Pending Acquisition

On December 18, 2006, the Company entered into an agreement and plan of reorganization (Agreement) by which it will acquire American Apparel. American Apparel is provider of cotton leisure wear geared toward contemporary metropolitan adults and sold through company-owned retail locations and online.

In exchange for a 100% equity of American Apparel, the Company will issue 32,258,065 shares of its common stock (Transaction Shares), subject to downward adjustment based on American Apparel s net debt immediately prior to closing of the acquisition. 8,064,516 of the Transaction Shares will be placed into escrow to secure the Company s indemnity rights under the Agreement. The Agreement also provides for a $2.5 million cash pool to be available for the granting of bonuses to management employees immediately following the closing of the acquisition. American Apparel also will be permitted to repay at the closing of the acquisition loans made to American Apparel by certain of its directors, officers and employees in an aggregate amount of approximately $15,000,000. The Company also will adopt a performance equity plan under which an aggregate of approximately 2,710,000 shares will be available for grant under options and restricted stock awards to employees.

The Company will submit such transaction for stockholder approval. The Company expects that the transaction will be consummated in December 2007, after the required approval by its stockholders. As of September 30, 2007, the Company has capitalized $431,314 of acquisition costs in connection with this acquisition. There can be no assurance that the acquisition will be completed.

Table of Contents

ENDEAVOR ACQUISITION CORP.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS (Continued)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006 AND

THE PERIOD JULY 22, 2005 (INCEPTION) TO SEPTEMBER 30, 2007

On November 6, 2007, the Company entered into an amended Acquisition Agreement (Amended Agreement) under which the number of transaction shares issued by the Company at the closing of the acquisition increased from 32,258,065 to 37,258,065 while at the same time increasing the level of American Apparel s net debt above which there would be a downward adjustment in the number of shares issued at the closing of the acquisition from $110 million to $150 million. The Amended Agreement also increased the size of the 2007 performance equity plan from 2,710,000 shares to 7,710,000 shares and provides that stock awards for an aggregate of 2,710,000 shares would be allocated and issued thereunder after consummation of the closing and upon filing of an effective registration statement.

9. Uncertain Tax Positions

Effective January 1, 2007, the Company adopted the provisions of the Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48). There were no unrecognized tax benefits as of January 1, 2007 and as of September 30, 2007. FIN 48 prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by taxing authorities. The Company has identified its federal tax return and its state tax return in New York as major tax jurisdictions, as defined in FIN 48. The Company s evaluations were performed for tax years ended 2005 and 2006, the only periods subject to examination. The Company believes that its income tax positions and deductions would be sustained on audit and does not anticipate any adjustments that would result in a material change to its financial position. The Company recognizes accrued interest and penalties related to unrecognized tax benefits as income tax expense. No amounts were accrued for the payment of interest and penalties at January 1, 2007. There was no change to this balance at September 30, 2007. The Company does not expect its unrecognized tax benefit position to change during the next twelve months. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position. The adoption of the provisions of FIN 48 did not have a material impact on the Company s financial position, results of operations and cash flows.

10. Subsequent Event

On October 17, 1007, the Company borrowed funds from two of the Company s officers. The Company issued two promissory notes in the amount of $50,000 each. The principal balance of these notes shall be repayable on the earlier of the consummation of the Company s business combination with American Apparel or upon demand by the officers. These promissory notes are non-interest bearing.

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of

Endeavor Acquisition Corp.

We have audited the accompanying balance sheets of Endeavor Acquisition Corp. (a development stage enterprise) (the Company) as of December 31, 2006 and 2005 and the related statements of operations, changes in stockholders equity and cash flows for the year ended December 31, 2006, for the period July 22, 2005 (inception) to December 31, 2005 and from July 22, 2005 (inception) to December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Endeavor Acquisition Corp. (a development stage enterprise) as of December 31, 2006 and 2005, and the results of its operations and its cash flows for the year ended December 31, 2006, for the period July 22, 2005 (inception) to December 31, 2005, and from July 22, 2005 (inception) to December 31, 2006, in conformity with United States generally accepted accounting principles.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the financial statements, the Company s certificate of incorporation provides for mandatory liquidation of the Company in the event that the Company does not consummate a business combination (as defined) prior to July 21, 2007 or December 21, 2007 if certain extension criteria have been satisfied. These conditions raise substantial doubt about its ability to continue as a going concern. Management s plans regarding those matters are described in Note 3. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2006, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 14, 2007 expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ Marcum & Kliegman LLP

March 14, 2007
Melville, New York

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Balance Sheet

	December 31, 2006	December 31, 2005
Assets		
Current assets:		
Cash	$ 166,527	$ 1,114,634
Cash held in Trust Fund	125,113,007	112,308,199
Prepaid expenses	116,738	187,457
Total current assets	125,396,272	113,640,290
Deferred acquisition costs	145,808	
Equipment, net of accumulated depreciation of $631	3,914	
Total assets	$ 125,545,994	$ 113,640,290
Liabilities and Stockholders Equity		
Current liabilities accrued expenses	$ 260,076	$ 64,641
Common stock, subject to possible conversion, 3,232,148 and 2,999,999 shares, respectively, at conversion value	25,021,696	22,460,921
Commitment and Contingencies		
Stockholders equity		
Preferred stock, $.0001 par value, authorized 1,000,000 shares; none issued		
Common stock, $.0001 par value; authorized 75,000,000 shares; total issued and outstanding 19,910,745 and 18,750,000 shares, respectively (less 3,232,148 and 2,999,999, respectively, subject to possible conversion)	1,668	1,575
Additional paid-in capital	97,338,103	91,058,838
Earnings accumulated during development stage	2,924,451	54,315
Total stockholders equity	100,264,222	91,114,728
Total liabilities and stockholders equity	$ 125,545,994	$ 113,640,290

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

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Statement of Operations

	For the Year Ended December 31, 2006	For the Period from July 22, 2005 (inception) to December 31, 2005	For the Period From July 22, 2005 (inception) to December 31, 2006
Revenue	$	$	$
General, selling and administrative expenses	1,101,412	63,233	1,164,645
Operating loss	(1,101,412)	(63,233)	(1,164,645)
Dividend income	3,974,013	118,199	4,092,212
Income before provision of income tax	2,872,601	54,966	2,927,567
Provision for income tax	2,465	651	3,116
Net income	2,870,136	54,315	2,924,451
Accretion of Trust Fund relating to Common Stock subject to possible conversion	(793,712)	(23,628)	(817,340)
Net income available to common stockholders	$ 2,076,424	$ 30,687	$ 2,107,111
Weighted average shares outstanding	16,668,534	4,670,245	12,836,677
Basic and diluted net income per share	$ 0.12	$ 0.01	$ 0.16

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

FS-134

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Statement of Changes in Stockholders Equity From July 22, 2005 (Inception)

to December 31, 2006

	Common Stock		Additional	Earnings Accumulated During	Total
			Paid-In	Development	Stockholders
	Shares	Amount	Capital	Stage	Equity
Balance, July 22, 2005 (inception)		$	$	$	$
Issuance of stock to initial stockholders	3,750,000	375	24,625		25,000
Sale of 15,000,000 units, net of underwriters discount and offering expenses of $6,503,766 (includes 2,999,999 shares subject to possible conversion)	15,000,000	1,500	113,494,734		113,496,234
Proceeds subject to possible conversion of 2,999,999 shares		(300)	(22,436,993)		(22,437,293)
Proceeds from issuance of options			100		100
Accretion of Trust Fund relating to Common Stock subject to possible conversion			(23,628)		(23,628)
Net income from July 22, 2005 (inception) to December 31, 2005				54,315	54,315
Balance, December 31, 2005	18,750,000	$ 1,575	$ 91,058,838	$ 54,315	$ 91,114,728
Sale of 1,160,745 units, net of underwriters discount and offering expenses of $445,726 (includes 232,149 shares subject to possible conversion)	1,160,745	116	8,840,117		8,840,233
Proceeds subject to possible conversion of 232,149 shares		(23)	(1,767,140)		(1,767,163)
Accretion of Trust Fund relating to Common Stock subject to possible conversion			(793,712)		(793,712)
Net income for the year ended December 31, 2006				2,870,136	2,870,136
Balance, December 31, 2006	19,910,745	$ 1,668	$ 97,338,103	$ 2,924,451	$ 100,264,222

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

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Statement of Cash Flows

	For the Year Ended December 31, 2006	For the Period from July 22, 2005 (inception) to December 31, 2005	For the Period from July 22, 2005 (inception to December 31, 2006
Cash Flows from Operating Activities			
Net income	$ 2,870,136	$ 54,315	$ 2,924,451
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Changes in operating assets and liabilities:			
Depreciation	631		631
Decrease (increase) of prepaid expenses	70,719	(187,457)	(116,738)
Increase in accrued expenses	195,435	64,641	260,076
Net cash provided by (used in) operating activities	3,136,921	(68,501)	3,068,420
Cash Flows from Investing Activities			
Purchase of equipment	(4,545)		(4,545)
Cash held in Trust Fund	(12,804,908)	(112,308,199)	(125,113,107)
Net cash used in investing activities	(12,809,453)	(112,308,199)	(125,117,652)
Cash Flows from Financing Activities			
Gross proceeds from initial public offering		120,000,000	120,000,000
Payment of deferred acquisition cost	(145,808)		(145,808)
Proceeds from sale of shares of common stock		25,000	25,000
Proceeds from the overallotment option	9,285,959		9,285,959
Proceeds from issuance of option		100	100
Payment of offering costs	(445,726)	(6,503,766)	(6,949,492)
Net cash provided by financing activities	8,694,425	113,521,334	122,215,759
Net (decrease) increase in cash	(978,107)	1,144,634	166,527
Cash at beginning of the period	1,144,634		
Cash at end of the period	$ 166,527	$ 1,114,634	$ 166,527

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

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements

1. Organization

Endeavor Acquisition Corp. (the Company) was incorporated in the State of Delaware on July 22, 2005 as a blank check company, whose objective is to acquire an operating business.

All activity from July 22, 2005 (inception) through December 21, 2005 related to the Company s formation and initial public offering. Since December 22, 2005, the Company has been searching for a target business to acquire. The Company has selected December 31 as its fiscal year end.

2. Business Operations

The Registration Statement for the Company s initial public offering (Offering) was declared effective December 15, 2005. The Company consummated the Offering on December 21, 2005 and received net proceeds of $113,496,234. In January 2006, the underwriter exercised the overallotment option generating an additional $8,840,233 of net proceeds. The Company s management has broad discretion with respect to the specific application of the net proceeds of the Offering, although substantially all of the net proceeds of the Offering are intended to be generally applied toward consummating a business combination with an operating business (Business Combination). Furthermore, there is no assurance that the Company will be able to successfully effect a Business Combination. An amount of $121,030,234 of the net proceeds from the initial public offering and the exercise of the underwriters overallotment option was deposited and is being held in an interest-bearing trust account (Trust Account) until the earlier of (i) the consummation of a Business Combination or (ii) liquidation of the Company. As of December 31, 2006, the balance in the Trust Account was $125,113,007, which includes $4,082,773 of dividend income. Under the agreement governing the Trust Account, funds will only be invested in United States government securities within the meaning of Section 2(a)(16) of the Investment Company Act of 1940, having a maturity of 180 days or less, or in money market funds meeting certain conditions under Rule 2a-7 promulgated under the Investment Company Act of 1940. The remaining net proceeds (not held in the Trust Account) may be used to pay for business, legal and accounting due diligence on prospective acquisitions and continuing general and administrative expenses.

The Company s Certificate of Incorporation provides for mandatory liquidation of the Company in the event that the Company does not consummate a Business Combination within 18 months from the date of the consummation of the Offering (July 21, 2007), or 24 months from the consummation of the Offering (December 21, 2007) if certain extension criteria have been satisfied. Such extension criteria have been satisfied. In the event of liquidation, it is likely that the per share value of the residual assets remaining available for distribution (including Trust Account assets) will be less than the initial public offering price per share in the Offering due to costs related to the Offering and since no value would be attributed to the Warrants contained in the Units sold.

All of the Company s stockholders prior to the Offering, including all of the officers and directors of the Company (Initial Stockholders), have agreed to

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements (Continued)

vote their 3,750,000 founding shares of common stock in accordance with the vote of the majority in interest of all other stockholders of the Company (Public Stockholders) with respect to any Business Combination. After consummation of a Business Combination, these voting safeguards will no longer be applicable.

3. Going Concern and Management Plans

As of December 31, 2006, the Company only has working capital of $23,189, net of $125,113,007 of which is cash held in Trust. On December 18, 2006 the Company entered into an agreement to acquire an operating entity expected to be consummated by the summer of 2007. In order for the Company to continue to fund the operating costs associated with the acquisition, the Company s officers have agreed to advance the Company enough capital in order to consummate the acquisition. There can be no assurance that the acquisition described in Note 10 will be consummated. Should this Business Combination, or another qualifying Business Combination, not be reduced to a definitive agreement and consummated, the Company would be required to return the funds held in the Trust Account to holders of shares issued in the Offering described in Note 5, as a mandatory liquidation, pursuant to a plan of dissolution and liquidation approved by stockholders. These conditions raise substantial doubt about the Company s ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

4. Significant Accounting Policies

Cash and Cash Equivalents

The Company considers all highly liquid instruments with maturities of three months or less to be cash equivalents.

Earnings Per Share

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is calculated by dividing net income available to common stockholders by the weighted-average number of shares of common stock and warrants outstanding during the period. The conversion of the outstanding warrants, totaling 16,160,745, is contingent upon the occurrence of future events, and therefore, is not includable in the calculation of diluted earnings per share in accordance with Statement of Financial Accounting Standards (SFAS) No. 128, Earnings per Share. Options to purchase 350,000 Units granted to the representative of the underwriters are not included in diluted earnings per share as their effect is antidilutive. Weighted average shares outstanding do not include the common stock subject to possible conversion.

Concentration of Credit Risk

SFAS No. 105, Disclosure of Information about Financial Instruments with Off-Balance Sheet Risk and Financial Instruments with Concentration of Credit Risk, requires disclosure of significant concentrations of credit risks

FS-138

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements (Continued)

regardless of the degree of risk. At December 31, 2006, financial instruments that potentially expose the Company to credit risk consist of cash. The Company maintains its cash balances in various financial institutions. The Federal Deposit Insurance Endeavor Acquisition Corp.

Corporation insures balances up to $100,000 and the Securities Investor Protection Corporation insures balances up to $500,000. At December 31, 2006, the uninsured balances amounted to approximately $124,916,822. Management believes the risk of loss to be minimal.

Fair Value of Financial Instruments

The carrying value of cash, cash held in Trust Fund and accrued expenses are reasonable estimates of the fair values due to their short-term maturity.

Estimates

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

Cash Held in Trust Account

The Company maintains its cash held in the Trust Account in tax free money market funds.

Recently Issued Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 155.

Accounting for Certain Hybrid Financial Instruments (SFAS 155), which eliminates the exemption from applying SFAS 133 to interests in securitized financial assets so that similar instruments are accounted for similarly regardless of the form of the instruments. SFAS 155 also allows the election of fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement event. Adoption is effective for all financial instruments acquired or issued after the beginning of the first fiscal year that begins after September 15, 2006.

Early adoption is permitted. The adoption of SFAS 155 is not expected to have a material effect on the Company s financial position, results of operations or cash flows.

In March 2006, the FASB issued SFAS No. 156 Accounting for Servicing of Financial Assets (SFAS 156), which requires all separately recognized servicing assets and servicing liabilities be initially measured at fair value. SFAS 156 permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. Adoption is required as

FS-139

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements (Continued)

of the beginning of the first fiscal year that begins after September 15, 2006. Early adoption is permitted. The adoption of SFAS 156 is not expected to have a material effect on the Company s financial position, results of operations or cash flows.

In July 2006, the FASB issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109 (FIN 48). FIN 48 clarifies the accounting and reporting for uncertainties in income tax law. This Interpretation prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. This Interpretation shall be effective for fiscal years beginning after December 15, 2006. The cumulative effects, if any, of applying this Interpretation will be recorded as an adjustment to retained earnings as of the beginning of the period of adoption. The Company has not yet commenced the process of evaluating the expected effect of FIN 48 on its financial statements and is not currently in a position to determine such effects.

In September 2006, the FASB issued SFAS No. 157 Fair Value Measurements (SFAS No. 157).

This Statement defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements and accordingly does not require any new fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company has not evaluated the potential impact, if any, of the adoption of SFAS No. 157 will have on its financial position, results of operations and cash flows.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin 108, Considering the Effects on Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 requires registrants to quantify errors using both the income statement method (i.e. iron curtain method) and the rollover method and requires adjustment if either method indicates a material error. If a correction in the current year relating to prior year errors is material to the current year, then the prior year financial information needs to be corrected. A correction to the prior year results that are not material to those years would not require a restatement process where prior financials would be amended. SAB 108 is effective for fiscal years ending after November 15, 2006. The Company has assessed SAB 108 and has concluded that it did not have a material effect on its financial position, results of operations or cash flows.

Income Taxes

Deferred income taxes are provided for the differences between the bases of assets and liabilities for financial reporting and income tax purposes. A

FS-140

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements (Continued)

valuation allowance is established when necessary to reduce deferred tax assets to the amount expected to be realized. Management did not record the impact of deferred taxes as they were deemed immaterial. The provision for Federal, state and local taxes, which are included in the accompanying statement of operations, amounted to $2,465 for the year ended December 31, 2006, $651 for the period from July 22, 2005 (Inception) to December 31, 2005, and $3,116 from July 22, 2005 (Inception) to December 31, 2006.

5. Initial Public Offering

On December 21, 2005, the Company sold 15,000,000 units (Units) in the Offering at $8.00 per Unit. Each Unit consists of one share of the Company s common stock, and one Redeemable Common Stock Purchase Warrant (Warrants). In January 2006, the underwriters exercised the overallotment option and an additional 1,160,745 units were sold. Each Warrant entitles the holder to purchase from the Company one share of common stock at an exercise price of $6.00 commencing the later of the completion of a Business Combination or December 15, 2006 and expiring on December 14, 2009. The Warrants will be redeemable by the Company, at a price of $.01 per Warrant upon 30 days notice after the Warrants become exercisable, only in the event that the last sale price of the common stock is at least $11.50 per share for any 20 trading days within a 30 trading day period ending on the third day prior to the date on which notice of redemption is given. In connection with this Offering, the Company issued an option, for $100, to Ladenburg Thalmann & Co. Inc., the representative of the underwriters in the Offering (Representative), to purchase 350,000 Units at an exercise price of $10.00 per Unit. The Company has accounted for the fair value of the option, inclusive of the receipt of the $100 cash payment, as an expense of the public offering resulting in a charge directly to stockholders equity. The Company estimates that the fair value of this option is approximately $703,500 ($2.01 per Unit) using a Black-Scholes option-pricing model. The fair value of the option granted to the Representative is estimated as of the date of grant using the following assumptions: (1) expected volatility of 52.7%, (2) risk-free interest rate of 4.43% and (3) expected life of two years and 30 days. The option may be exercised for cash or on a cashless basis at the holder s option, such that the holder may use the appreciated value of the option (the difference between the exercise prices of the option and the underlying Warrants and the market price of the Units and underlying securities) to exercise the option without the payment of any cash.

6. Notes Payable, Stockholders

In July 2005, the Company issued an aggregate of $225,000 unsecured promissory note to its executive officers. The notes were non interest-bearing and were paid in full upon the consummation of the Offering from the net proceeds of the Offering.

7. Commitment and Contingencies

The Company presently occupies office space provided by an affiliate of one of the Company s executive officers. Such affiliate has agreed that, until the consummation of a Business Combination, it will make such office space, as well as certain office and secretarial services, available to the Company, as may be required by the Company from time to time. The Company has agreed to pay such affiliate $7,500 per month for such services commencing on the

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements (Continued)

effective date of the Offering. The statement of operations for the year ended December 31, 2006, for the period from July 22, 2005 (Inception) to December 31, 2005 and from July 22, 2005 (Inception) to December 31, 2006, includes $90,000, $2,500 and $92,500, respectively, related to this agreement.

Pursuant to letter agreements with the Company and the Representative, the Initial Stockholders have waived their right to receive distributions with respect to their founding shares upon the Company s liquidation.

The Initial Stockholders are entitled to registration rights with respect to their founding shares pursuant to an agreement dated December 15, 2005. The holders of the majority of these shares are entitled to make up to two demands that the Company register these shares at any time commencing three months prior to the third anniversary of the effective date of the Offering. In addition, the Initial Stockholders have certain piggy-back registration rights on registration statements filed subsequent to the third anniversary of the effective date of the Offering.

The Company hired a consultant on July 17, 2006 to perform services through the later of June 15, 2007 if the Company has not announced an acquisition candidate within the initial 18 month period or December 15, 2007 if the Company has signed a letter of intent with a proposed acquisition candidate within the initial 18 month period. The Company will pay the consultant a base salary of $125,000 per year and the Company will issue to the consultant 12,500 shares of the Company s common stock upon the closing of the initial Business Combination by the Company. The Company will also issue to the consultant an additional 12,500 shares of the Company s common stock six months after closing of the initial Business Combination by the Company.

8. Preferred Stock

The Company is authorized to issue 1,000,000 shares of preferred stock with such designations, voting and other rights and preferences as may be determined from time to time by the Board of Directors.

9. Common Stock

Effective November 21, 2005, two of the Initial Stockholders contributed an aggregate of 2,500,000 shares of common stock, at no cost, to the Company. All references in the accompanying financial statements to the number of shares of common stock have been retroactively restated to reflect this transaction.

On January 4, 2006 the underwriters informed the Company of their desire to exercise the over-allotment option to the extent of 1,160,745 Units. Gross proceeds amounted to $9,285,959, there was a $445,726 underwriting discount and the remainder of $8,840,233 was deposited in the Trust Account.

At December 31, 2006, 16,860,745 shares of common stock were reserved for issuance upon exercise of redeemable warrants and the underwriters unit purchase option.

10. Pending Acquisition

On December 18, 2006, the Company entered into an agreement and plan of reorganization (Agreement) by which it will acquire American Apparel,

Table of Contents

Endeavor Acquisition Corp.

(a development stage enterprise)

Notes to Financial Statements (Continued)

Inc. and its affiliated companies (collectively, American Apparel). American Apparel is provider of cotton leisure wear geared toward contemporary metropolitan adults and sold through company-owned retail locations and online.

In exchange for a 100% equity of American Apparel, the Company will issue 32,258,065 shares of its common stock (Transaction Shares), subject to downward adjustment based on American Apparel s net debt immediately prior to closing of the acquisition. 8,064,516 of the Transaction Shares will be placed into escrow to secure the Company s indemnity rights under the Agreement. The Agreement also provides for a $2.5 million cash pool to be available for the granting of bonuses to management employees immediately following the closing of the acquisition. American Apparel also will be permitted to repay at the closing of the acquisition loans made to American Apparel by certain of its directors, officers and employees in an aggregate amount of approximately $5 million. The Company also will adopt a performance equity plan under which an aggregate of approximately 2.7 million shares will be available for grant under options and restricted stock awards to employees.

The Company will submit such transaction for stockholder approval. The Company expects that the transaction will be consummated in the Summer of 2007, after the required approval by its stockholders. As of December 31, 2006, the Company has capitalized $145,808 of acquisition costs in connection with this acquisition. There can be no assurance that the acquisition will be completed.

Table of Contents

Annex A

AMENDED AND RESTATED

AGREEMENT AND PLAN OF REORGANIZATION

BY AND AMONG

ENDEAVOR ACQUISITION CORP.,

(Parent)

AAI ACQUISITION LLC,

(Merger Sub)

AMERICAN APPAREL INC.,

(AAI)

AMERICAN APPAREL, LLC,

(LLC)

EACH OF THE CANADIAN COMPANIES SET FORTH ON SCHEDULE A HERETO,

(all of such companies collectively referred to as CI)

DOV CHARNEY

(Stockholder)

and

WITH RESPECT TO CERTAIN PROVISIONS ONLY,

EACH OF THE STOCKHOLDERS OF CI

(collectively, the CI Stockholders)

and

WITH RESPECT TO CERTAIN PROVISIONS ONLY,

SAM LIM

(Lim)

ORIGINALLY EXECUTED AS OF DECEMBER 18, 2006

AMENDED AND RESTATED AS OF NOVEMBER 7, 2007

A-1

Table of Contents

AMENDED AND RESTATED AGREEMENT AND PLAN OF REORGANIZATION

THIS AMENDED AND RESTATED AGREEMENT AND PLAN OF REORGANIZATION is made and entered into as of November 7, 2007, by and among:

Endeavor Acquisition Corp., a Delaware corporation (*Parent*);

AAI Acquisition LLC, a California limited liability company and a wholly-owned subsidiary of Parent (*Merger Sub*);

American Apparel Inc., a California corporation (*AAI*);

American Apparel, LLC, a California limited liability company (*LLC* and, collectively with AAI and CI, the *Company*);

Each of the corporations (each an affiliate of AAI and/or the Stockholder) formed under the laws of the applicable provinces of Canada or the Canada Business Corporation Act as set forth on *Schedule A* hereto (each such company referred to herein as a *CI company* and all of such companies referred to collectively herein as *CI* or the *CI companies*);

Dov Charney, an owner of 50% of the outstanding capital stock of AAI and 50% of the outstanding membership interests of LLC (the *Stockholder*);

Sang Ho Lim, the current owner of the remaining 50% of the outstanding capital stock of AAI and the remaining 50% of the outstanding membership interests of LLC (*Lim*), joins this Agreement as a party solely for purposes of Sections 1.1(a), 1.5(a), 1.6, 1.7, 1.8, 1.9, 1.10 1.12(a), 1.12(c), 1.15, 2.3(a), 2.3(c), 2.4(a), 2.4(c), 2.5(b), 2.24, 4.1(f), 4.2, 5.6, 5.8(c), 5.9, 5.11, 5.12, 5.13, 5.14(b), 5.17, 5.26, 5.27, 5.28, Article VIII, Article IX and Article X; and

Each person executing the CI Stockholder Signature Page to this Agreement, being (a) the owner or (b) the registered nominee or holder representing the owner with no beneficial interest vested in themselves, as the case and context may require herein, of all of the outstanding capital stock of each of the CI companies (*CI Stockholders*), joins this Agreement as a party solely for purposes of Sections 1.1(b), 1.5(a), 1.5(b), 1.6, 1.7, 1.8, 1.9, 1.12, 2.3(b), 2.4(a), 2.4(c), 2.24, 4.1(f), 4.2, 5.6, 5.8(c), 5.9, 5.10, 5.11, 5.12, 5.13, 5.14(b), 5.17, Article VIII, Article IX and Article X.

This Agreement amends and restates the Agreement and Plan of Reorganization, dated as of December 18, 2006 (*December 2006 Agreement*), by and among Parent, AAI Acquisition Corp., a California corporation and a wholly owned subsidiary of Parent, AAI, LLC, each of the corporations formed under the laws of the applicable provinces of Canada or the Canada Business Corporation Act as set forth on Schedule A thereto, the Stockholder, Lim and each person executing the CI Stockholder Signature Page thereto. Notwithstanding anything to the contrary, all representations and warranties contained herein and all schedules referenced herein and made a part hereto shall be deemed to be made and speak as of December 18, 2006, except *Schedules A*, *1.2*, *1.5(a)*, *2.1(a)*, *2.1(b)*, *2.3(b)*, *2.22* and *5.25(c)* as attached hereto (collectively, the *Amended Schedules*), which shall be deemed to speak as of the date hereof. It is acknowledged by the Parties that AAI Acquisition Corp. has withdrawn as a party to the Agreement and has been replaced by AAI Acquisition LLC which as of the date hereof has become a party to this Agreement. All schedules and exhibits delivered with the December 2006 Agreement shall be deemed incorporated by reference herein and are made a part hereof, other than *Schedules A*, *1.2*, *1.5(a)*, *2.1(a)*, *2.1(b)*, *2.3(b)*, *2.22* and *5.25(c)* and *Exhibit F*, which are replaced by the Amended Schedules and the new *Exhibit F* being delivered concurrently with the execution of this Agreement.

The term *Agreement* as used herein refers to this Agreement and Plan of Reorganization, as the same may be amended from time to time, and all schedules hereto (including the Company Schedule and the Parent Schedule, as defined in the preambles to Articles II and III hereof, respectively).

A-2

Table of Contents

RECITALS

A. Upon the terms and subject to the conditions of this Agreement (as defined in Section 1.2) and in accordance with the applicable corporate and limited liability laws of the respective jurisdictions of formation of each of the companies as set forth in the preamble of this Agreement (the *Applicable Corporate Laws*), Parent and the Company intend to enter into a business combination transaction by means of a concurrent (i) merger in which Merger Sub will merge with AAI and be the surviving entity and (ii) acquisition by Parent of all of the outstanding capital stock of each of the CI companies, through an exchange of all the issued and outstanding shares of capital stock of each of AAI and each CI company for shares of common stock of Parent.

B. Immediately prior to the closing of the Business Combination (as defined in Section 1.1), all of the then outstanding membership interests of LLC shall be transferred to AAI.

C. Between the date of this Agreement and the Closing, if the Stockholder so elects, the Stockholder shall purchase from Lim (and if the Stockholder does not so purchase from Lim, then Parent shall purchase from Lim at the Closing) all of Lim s Company Capital Stock (as defined) and Company Membership Interests (as defined) under the terms of this Agreement and on the terms set forth in the Lim Option Agreement (as defined), as the same may be modified by this Agreement.

D. The Boards of Directors of AAI, each CI company and Parent and the managers of Merger Sub and LLC have determined that the Business Combination is fair to, and in the best interests of, their respective companies and stockholders and members, as applicable.

E. The parties intend that this Agreement shall constitute a plan of reorganization within the meaning of section 368 of the Internal Revenue Code of 1986, as amended (the *Code*) in respect of the Merger and each of the Canada Acquisitions (as defined).

NOW, THEREFORE, in consideration of the covenants, promises and representations set forth herein, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties agree as follows (defined terms used in this Agreement are listed alphabetically in Article IX, together with the Section and, if applicable, paragraph number in which the definition of each such term is located):

ARTICLE I

THE MERGER AND RELATED ACQUISITIONS

1.1 *The Business Combination*. At the Effective Time (as defined in Section 1.2) and subject to and upon the terms and conditions of this Agreement and the Applicable Corporate Laws:

(a) AAI shall be merged with and into Merger Sub (the *Merger*), the separate corporate existence of AAI shall cease and Merger Sub shall continue as the surviving corporation. Merger Sub as the surviving corporation after the Merger is hereinafter sometimes referred to as the *U.S. Surviving Corporation*.

(b) All of the outstanding capital stock of each CI company shall be acquired by Parent (each, a *Canada Acquisition*, and together, the *Canada Acquisitions* and, collectively with the Merger, the *Business Combination*), and the separate corporate existence of each CI company shall continue, with each such company a wholly owned subsidiary of Parent.

1.2 *Effective Time; Closing*. Subject to the conditions of this Agreement, the parties hereto shall cause the Business Combination to be consummated by filing as soon as practicable on or after the Closing Date (as herein defined) with each jurisdiction set forth on *Schedule 1.2* hereto the certificates, articles, forms and other documentation necessary to consummate the Merger, the Canada Acquisitions and related transactions (including, but not limited to, any notices, stock transfer forms and payment of any transfer, stamp or duty taxes)

described on *Schedule 1.2* in accordance with the Applicable Corporate Laws (collectively, the *Transaction Certificates*). The time of the last such filing to be properly completed or such later time as may be agreed in writing by Parent and the Company shall be referred to herein as the *Effective Time*. Unless this Agreement has been terminated pursuant to Section 8.1, the closing of the Business Combination (the *Closing*) shall take place concurrently at the offices of Graubard Miller, counsel to Parent, 405 Lexington Avenue, New York, New York 10174-1901 at a time and date to be specified by the parties, which shall be no later than the second business day after the satisfaction or waiver of the conditions set forth in Article VI, or at such other time, date and location as the parties hereto agree in writing (the *Closing Date*). Closing signatures may be transmitted by facsimile.

1.3 *Effect of the Business Combination*. At the Effective Time, the effect of the Business Combination shall be as provided in this Agreement and the provisions of the Applicable Corporate Laws. Without limiting the generality of the foregoing, and subject thereto, at the Effective Time:

(a) All the property, rights, privileges, powers and franchises of AAI and Merger Sub shall vest in U.S. Surviving Corporation, and all debts, liabilities and duties of AAI and Merger Sub shall become the debts, liabilities and duties of U.S. Surviving Corporation; and

(b) Each of the CI companies shall remain in existence and shall continue after the Business Combination as a wholly owned subsidiary of Parent.

1.4 *Charter Documents*.

(a) At the Effective Time:

(i) the Articles of Incorporation of Merger Sub shall be the Articles of Incorporation of U.S. Surviving Corporation.

(ii) the Articles of Incorporation of each CI company shall remain the Articles of Incorporation of such CI company.

(b) At the Effective Time:

(i) the Bylaws of Merger Sub shall be the Bylaws of U.S. Surviving Corporation.

(ii) the Articles of Association of each CI company shall remain the Articles of Association of such CI company.

1.5 *Effect on Capital Stock*. Subject to the terms and conditions of this Agreement, at the Effective Time, by virtue of the Business Combination and this Agreement and without any action on the part of any party hereto, the following shall occur:

(a) *Conversion or Exchange of Company Capital Stock*. Other than any shares to be canceled pursuant to Section 1.5(c), and subject to Section 1.5(b) and Section 5.28 of this Agreement, on the Closing Date, (i) all of the shares of capital stock of AAI issued and outstanding immediately prior to the Effective Time held by the holders thereof will be automatically converted into the right to receive, and (ii) all of the shares of capital stock of each CI company will be exchanged for, an aggregate of 37,258,065 shares (*Transaction Shares*) of the common stock, par value $0.0001, of Parent (*Parent Common Stock*). The Transaction Shares are also sometimes referred to herein as the *Transaction Consideration*. The Transaction Shares shall be issued and allocated in accordance with an allocation schedule to be attached hereto as *Schedule 1.5(a)* which shall be finalized as reasonably determined by the parties prior to the Closing, and shall be transferred solely to the Stockholder (as the beneficial owner, effective as of the Closing, of all of the outstanding capital stock of AAI and each of the CI companies) and his designees; provided, however, that 8,064,516 of the Transaction Shares (*Escrow Shares*) shall be placed in escrow as described in Section 1.11. No Transaction Shares shall be issued or transferred to any such designee unless such Person shall have delivered to Parent in writing (1) the investment representations set forth in Section 1.12(b) of this Agreement and (2) an agreement to be bound by a lock-up agreement, escrow agreements and voting agreement having the same terms as the lock-up agreement, escrow agreements and voting agreement

executed by the Stockholder in connection with the Business Combination (other than such changes as are necessary to reflect that such designee and not the Stockholder is the party thereto). All of the shares of capital stock of AAI and each CI company and each of their respective Subsidiaries shall be referred to collectively herein as the *Company Capital Stock*. Notwithstanding anything to the contrary, no such designee or designees shall be allocated Transaction Shares if such allocation shall require the filing of a registration statement under the Securities Act of 1933, as amended, or otherwise require any other filing (other than abbreviated or notice filings) or otherwise serve to eliminate any registration exemption otherwise available to Parent had the Transaction Shares been issued only to the Stockholder or serve to materially delay or prevent the consummation of the transactions contemplated hereby.

(b) *Net Debt and Reduction of Amount of Transaction Shares*.

(i) If the Company s Net Debt (as defined) at the close of business on the date two business days prior to the Closing Date (*Closing Date Net Debt*) is more than $150,000,000 as determined in accordance with this Agreement, the number of Transaction Shares to be issued at the Closing shall be reduced by that number of shares equal to the Net Debt Transaction Share Reduction Number. Except for debt incurred to pay any Stub Period Tax Amounts (including, without limitation, any notes issued by AAI to pay any Stub Period Tax Amounts), the Company shall not incur any debt, other than in the ordinary course of business during the period from the date two business days prior to the Closing Date and the Closing Date.

(ii) The term *Net Debt Transaction Share Reduction Number* shall mean the quotient derived by dividing (i) the difference between the Closing Date Net Debt and $150,000,000 by (ii) $7.75 (rounded up to the nearest share); provided, however, that if Closing Date Net Debt is equal to or less than $150,000,000, the Net Debt Transaction Share Reduction Number shall be zero.

(iii) The term Net Debt shall mean the Company s combined indebtedness (*i.e*., all indebtedness for borrowed money and capitalized leases and equivalents and other obligations evidenced by promissory notes or similar instruments, as well as cash overdrafts), less the Company s combined cash and cash equivalents (*i.e.,* all short-term money market instruments and treasury bills and similar instruments). The term Net Debt shall not include any debt incurred to pay any Stub Period Tax Amounts (including, without limitation, any notes issued by AAI to pay any Stub Period Tax Amounts).

(iv) From the date hereof through the Closing Date, on the 30th day of each calendar month, the Company shall deliver to Parent a written statement of the Company s Net Debt as of the end of the immediately preceding calendar month (*Periodic Net Debt Statement*), which shall (a) provide such detailed information as may be reasonably requested by Parent prior to such date, (b) be derived utilizing generally accepted accounting principles and (c) be certified as being true and complete by the Company s Chief Executive Officer and Chief Accounting Officer. On the business day prior to the scheduled Closing Date, the Company shall deliver to Parent a written statement of the Company s Net Debt as of the close of business of the immediately prior business day (*Closing Net Debt Statement*), which shall (a) provide such detailed information as may be reasonably requested by Parent prior to such date, (b) be derived utilizing generally accepted accounting principles and (c) be certified as being true and complete by the Company s Chief Executive Officer and Chief Financial Officer.

(c) *Cancellation of Treasury and Parent-Owned Stock.* Each share of Company Capital Stock held by the Company or Parent or any direct or indirect wholly-owned subsidiary thereof immediately prior to the Effective Time shall be canceled and extinguished without any conversion or payment in respect thereof.

(d) *Adjustments to Exchange Ratios.* The numbers of shares of Parent Common Stock that the beneficial holders of the Company Capital Stock are entitled to receive as a result of the Business Combination shall be equitably adjusted to reflect appropriately the effect of any stock split, reverse stock split, stock dividend (including any dividend or distribution of securities convertible into Parent Common Stock), reorganization, recapitalization, reclassification, combination, exchange of shares or other like change with respect to Parent Common Stock or Company Capital Stock occurring on or after the date hereof and prior to the date of issuance or payments thereof.

Table of Contents

(e) *Fractional Shares.* No fraction of a share of Parent Common Stock will be issued by virtue of the Business Combination, and each holder of shares of Company Capital Stock who would otherwise be entitled to a fraction of a share of Parent Common Stock (after aggregating all fractional shares of Parent Common Stock that otherwise would be received by such holder) shall, upon compliance with Section 1.6, receive from Parent, in lieu of such fractional share, one (1) share of Parent Common Stock.

1.6 *Surrender of Certificates; Uncertificated Shares*.

(a) *Exchange Procedures*. Upon surrender of all of the certificates representing Company Capital Stock (*Company Certificates*) at the Closing, the holders of such Company Certificates shall receive in exchange therefor certificates representing the Transaction Shares into which their shares of Company Capital Stock shall be converted or exchanged at the Effective Time, less the Escrow Shares. Until so surrendered, outstanding Company Certificates will be deemed, from and after the Effective Time, to evidence only the right to receive the applicable portion of the Transaction Shares then issuable under the terms of this Agreement. Subject to compliance with United States federal backup withholding rules and the Canadian tax clearance certificate regime set forth in Section 1.6(d) hereof, the parties hereto acknowledge and agree that, as of the date hereof, no such deduction or withholding would be required by applicable law.

(b) *Required Withholding*. The Parent and the Surviving Corporations shall be entitled to deduct and withhold from any consideration payable or otherwise deliverable pursuant to this Agreement to any holder or former holder of Company Capital Stock such amounts as are required to be deducted or withheld therefrom under the Code or under any provision of state, local or foreign tax law or under any other applicable legal requirement. To the extent such amounts are so deducted or withheld, such amounts shall be treated for all purposes under this Agreement as having been paid to the person to whom such amounts would otherwise have been paid.

(c) *No Liability.* Notwithstanding anything to the contrary in this Section 1.6, neither Parent, U.S. Surviving Corporation, the Company nor any other party hereto shall be liable to a holder of shares of Parent Common Stock or Company Capital Stock for any amount properly paid to a public official pursuant to any applicable abandoned property, escheat or similar law.

(d) *Canadian Tax Clearance Certificate.* The following provisions apply in respect of each disposition of the shares of a CI company by CI Stockholders to Parent (the *Recipient Party*) pursuant to this Agreement:

(i) Subject to the remaining provisions of this Section 1.6(d), the CI Stockholders will deliver to Recipient Party a certificate issued pursuant to section 116 of the *Income Tax Act* (Canada) (*Canadian Tax Act*) in respect of the disposition of the shares of the relevant CI company to the Recipient Party (*Section 116 Certificate*).

(ii) If no Section 116 Certificate is delivered to the Recipient Party on or prior to the Closing Date, the Recipient Party shall withhold 25% of the portion of the Transaction Shares that is allocable to the acquisition of the shares of the CI company (such shares hereinafter referred to as the *Canadian Shares* and such portion hereinafter referred to as the *Canadian Allocation*). Such withheld Transaction Shares will be dealt with as provided for in Section 1.6(d)(iv).

(iii) If a certificate issued by the Minister of National Revenue pursuant to subsection 116(2) of the Canadian Tax Act in respect of the transfer of the Canadian Shares to the Recipient Party is delivered to the Recipient Party on or prior to the Closing Date specifying a certificate limit in an amount less than the Canadian Allocation, the Recipient Party shall withhold from the Transaction Shares to be delivered at Closing that number of Transaction Shares that has a value equal to 25% of the amount by which the Canadian Allocation exceeds the certificate limit. Such withheld Transaction Shares will be dealt with as provided for in Section 1.6(d)(iv).

(iv) Any Transaction Shares withheld by the Purchaser pursuant to Section 1.6(d)(ii) or Section 1.6(d)(iii) (*Canadian Escrow Shares*) shall not be delivered to the CI stockholder at Closing and shall be held in escrow by Parent and only dealt with as hereinafter provided.

Table of Contents

(v) Subject to Section 1.6(d)(vii), if, prior to the 27th day after the end of the month in which the Closing Date occurs (*Due Date*) the CI Stockholder delivers to Recipient Party a Section 116 Certificate, the Recipient Party will deliver such CI Stockholder the Canadian Escrow Shares other than that number of Canadian Escrow Shares that has a value equal to 25% of the amount by which the Canadian Allocation exceeds the certificate limit.

(vi) Subject to Section 1.6(d)(vii), if Recipient Party has withheld Transaction Shares pursuant to Section 1.6(d)(ii) or Section 1.6(d)(iii) and the CI stockholder does not deliver to the Recipient Party, prior to the Due Date, a Section 116 Certificate or delivers a Section 116 Certificate specifying a certificate limit less than the Canadian Allocation, the Recipient Party or, at its election, the CI Stockholder shall remit to the Receiver General of Canada that number of Canadian Escrow Shares or, in the case of the CI Stockholder, any other property or assets that have an aggregate value equal to the amount required to be remitted pursuant to subsection 116(5) of the Canadian Tax Act and shall provide evidence of such remittance to the CI Stockholder. The Recipient Party shall cause to be delivered to the CI Stockholder any remaining portion of the Canadian Escrow Shares.

(vii) The Due Date under Section 1.6(d)(v) and Section 1.6(d)(vi) may be extended to a later date if the Canada Revenue Agency confirms in writing to Recipient Party that Recipient Party may continue to hold the Canadian Escrow Shares without being subject to penalty and interest for late remittance, provided that a copy of such correspondence is delivered to the Recipient Party.

1.7 *No Further Ownership Rights in Company Stock*. All shares of Parent Common Stock issued in accordance with the terms hereof shall be deemed to have been issued in full satisfaction of all rights pertaining to such shares of Company Capital Stock and there shall be no further registration of transfers on the records of the Surviving Corporations or the Company of shares of Company Capital Stock that were outstanding immediately prior to the Effective Time. If, after the Effective Time, Company Certificates are presented to Parent or any Surviving Corporation for any reason, they shall be canceled and exchanged as provided in this Article I.

1.8 *Lost, Stolen or Destroyed Certificates*. In the event that any Company Certificates shall have been lost, stolen or destroyed, Parent shall issue in exchange for such lost, stolen or destroyed Company Certificates, upon the making of an affidavit of that fact by the holder thereof, the certificates representing the shares of Parent Common Stock into which the shares of Company Capital Stock formerly represented by such Company Certificates were converted or exchanged; provided, however, that, as a condition precedent to the issuance of such certificates representing shares of Parent Common Stock, the owner of such lost, stolen or destroyed Company Certificates shall indemnify Parent against any claim that may be made against Parent or U.S. Surviving Corporation with respect to the Company Certificates alleged to have been lost, stolen or destroyed.

1.9 *Tax Consequences*. It is intended by the parties hereto that the Merger and each Canada Acquisition shall constitute a reorganization within the meaning of Section 368 of the Code. The parties hereto adopt this Agreement as a plan of reorganization for the Merger and each Canada Acquisition within the meaning of Sections 1.368-2(g) and 1.368-3(a) of the United States Income Tax Regulations.

1.10 *Taking of Necessary Action; Further Action*. If, at any time after the Effective Time, any further action is necessary or desirable to carry out the purposes of this Agreement and to vest (a) U.S. Surviving Corporation with full right, title and possession to all assets, property, rights, privileges, powers and franchises of AAI, LLC and Merger Sub and (b) Parent with the full right, title and possession to all shares of capital stock of each CI company, the officers and directors of AAI, LLC and Merger Sub will take all such lawful and necessary action.

1.11 *Escrow*. As the sole remedy for the indemnity obligations set forth in Article VII, at the Closing, the Stockholder shall deposit in escrow, to be held from the Closing Date until the later of (i) the first anniversary of the Closing Date and (ii) 30 days after Parent has filed with the SEC its annual report on Form 10-K or 10-KSB for the year ending December 31, 2007 (such period, the *Escrow Period*), and for such further period as may

Table of Contents

be required pursuant to the Escrow Agreement referred to below, an aggregate of 8,064,516 Escrow Shares, all in accordance with the terms and conditions of the Escrow Agreement to be entered into at the Closing between Parent, the Stockholder and Continental Stock Transfer & Trust Company, as escrow agent (*Escrow Agent*), in the form annexed hereto as *Exhibit A* (the *Escrow Agreement*).

1.12 *Stockholder Matters*.

(a) By his, her or its execution of this Agreement, the Stockholder and each of the CI Stockholders and Lim, in his, her or its capacity as a registered or beneficial stockholder of AAI and/or CI, and/or as a member of LLC, hereby approves and adopts this Agreement and authorizes each of AAI, each CI company and LLC, its respective directors, managers and officers to take all actions necessary for the consummation of the Business Combination and the other transactions contemplated hereby pursuant to the terms of this Agreement and its exhibits. Such execution shall be deemed to be action taken by the irrevocable written consent of the Stockholder, the CI Stockholders and Lim for purposes of the Applicable Corporate Laws. The Stockholder, each of the CI Stockholders and Lim also confirms that he, she or it is not entitled to any appraisal, dissenters or similar rights pursuant to the Applicable Corporate Laws.

(b) The Stockholder and each of the CI Stockholders, severally and not jointly, represents and warrants as follows: (i) all Parent Common Stock to be acquired by such Person pursuant to this Agreement will be acquired for his, her or its account and not with a view towards distribution thereof other than, with respect to any such Persons that are entities, transfers to its stockholders, partners or members; (ii) he, she or it understands that he, she or it must bear the economic risk of the investment in the Parent Common Stock, which cannot be sold by him, her or it unless it is registered under the Securities Act, or an exemption therefrom is available thereunder; (iii) he, she or it has had both the opportunity to ask questions and receive answers from the officers and directors of Parent and all persons acting on Parent s behalf concerning the business and operations of Parent and to obtain any additional information to the extent Parent possesses or may possess such information or can acquire it without unreasonable effort or expense necessary to verify the accuracy of such information; and (iv) he, she or it has had access to the Parent SEC Reports filed prior to the date of this Agreement. The Stockholder and each of the CI Stockholders acknowledges, as to himself, herself or itself only, that (v) he, she or it is either (A) an accredited investor as such term is defined in Rule 501(a) promulgated under the Securities Act or (B) a person possessing sufficient knowledge and experience in financial and business matters to enable it to evaluate the merits and risks of an investment in Parent; and (vi) he, she or it understands that the certificates representing the Parent Common Stock to be received by him, her or it may bear legends to the effect that the Parent Common Stock may not be transferred except upon compliance with (C) the registration requirements of the Securities Act (or an exemption therefrom) and (D) the provisions of this Agreement. Any CI Stockholder that is an entity, for itself, represents, warrants and acknowledges, with respect to each holder of its equity interests, to the same effect as the foregoing provisions of this Section 1.12(b).

(c) The Stockholder, each of the CI Stockholders and Lim, severally and not jointly, represents and warrants that the execution and delivery of this Agreement by such Person does not, and the performance of his, her or its obligations hereunder will not, require any consent, approval, authorization or permit of, or filing with or notification to, any court, administrative agency, commission, governmental or regulatory authority, domestic or foreign (a *Governmental Entity*), except (i) for applicable requirements, if any, of the Securities Act, the Securities Exchange Act of 1934, as amended (*Exchange Act*), state securities laws (*Blue Sky Laws*), and the rules and regulations thereunder, and (ii) where the failure to obtain such consents, approvals, authorizations or permits, or to make such filings or notifications, would not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect (as defined in Section 10.2(a)) on such Person or the Company or, after the Closing, the Parent, or prevent consummation of the Business Combination or otherwise prevent the parties hereto from performing their obligations under this Agreement.

Table of Contents

1.13 *Appointed Director for Purposes of Escrow Agreement.* At or prior to the Closing, the Board of Directors of Parent shall appoint one of its existing members (*Appointed Director*) who will continue to serve on Parent s board following consummation of the Business Combination under the terms of the Voting Agreement to act on behalf of Parent and to take all necessary actions and make all decisions following the Closing pursuant to the Escrow Agreement regarding Parent s rights under Article VII hereof. In the event the Appointed Director resigns from the Board, he shall have the right to appoint another member of the Board of Directors of Parent who was a director of Parent prior to the Closing Date or some other Person who would qualify as an independent director of Parent and who has not had any compensatory business relationship with the Company prior to the Closing to serve as his successor in the role of Appointed Director.

1.14 *Certain Registration Rights*. At the Closing, Parent and the Stockholder shall execute and deliver a Registration Rights Agreement in the form annexed hereto as *Exhibit B* with respect to registration of the Transaction Shares (the *Registration Rights Agreement*).

1.15 *Stub Period Tax Distributions*. Prior to the Lim Buy Out, there shall be distributed by AAI to each of the Stockholder and Lim in accordance with their pro rata interests in AAI, an amount equal to AAI s net taxable income for the period commencing January 1, 2006 and ending on the date of the distribution (the *Distribution Date*), multiplied by (B) the highest combined marginal Federal and state tax rate applicable to individuals residing in the State of California with respect to such income or gain (taking into account the amount and character of the income or gain) minus (C) all previous tax distributions made by AAI to the Stockholder and Lim in respect of the 2006 and 2007 taxable years, prior to the Distribution Date (the *Stub Period Tax Amounts*). The Stub Period Tax Amounts shall be payable by AAI in cash or in notes issued by AAI to the extent cash is not available, which notes shall be repaid as soon as practicable after Closing.

ARTICLE II

REPRESENTATIONS AND WARRANTIES REGARDING THE COMPANY

Subject to the exceptions set forth in *Schedule 2* attached hereto (the *Company Schedule*), each of the Company and the Stockholder severally and jointly represents and warrants to, and covenants with, Parent and Merger Sub, as set forth below in this Article II. In addition, Lim, solely with respect to himself, represents and warrants to, and covenants with, Parent and Merger Sub as set forth below in Section 2.3(a), 2.3 (c), 2.4(a), 2.4(c), 2.5(b) and 2.24. In addition, each of the CI Stockholders (other than the Stockholder), solely with respect to himself, herself or itself, represents and warrants to, and covenants with, Parent and Merger Sub as set forth below in Sections 2.3(b), 2.4(a), 2.4(c) and 2.24. As used in this Article II, and elsewhere in this Agreement, the term Company includes AAI, CI, LLC and their respective Subsidiaries, as hereinafter defined, unless the context clearly otherwise indicates.

2.1 *Organization and Qualification*.

(a) Each of AAI and each CI company is a corporation, and LLC is a limited liability company, duly organized, validly existing and in good standing under the laws of the state of its formation and has the requisite corporate or limited liability company power, as the case may be, and authority to own, lease and operate its assets and properties and to carry on its business as it is now being or currently planned by the Company to be conducted. The jurisdiction of formation of each of AAI, each CI company and LLC is as set forth on *Schedule 2.1(a)* hereto. The Company is in possession of all franchises, grants, authorizations, licenses, permits, easements, consents, certificates, approvals and orders (*Approvals*) necessary to own, lease and operate the properties it purports to own, operate or lease and to carry on its business as it is now being or currently planned by the Company to be conducted, except where the failure to have such Approvals could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on the Company. Complete and correct copies of the certificate or articles of incorporation, certificate or articles of formation, by-laws and operating agreements (or other comparable governing instruments with

Table of Contents

different names) (collectively referred to herein as *Charter Documents*) of each of AAI, each CI company and LLC (and their respective Subsidiaries), as amended and currently in effect, have been heretofore delivered to Parent or Parent s counsel. The Company is not in violation of any of the provisions of any of the Charter Documents. AAI, LLC and each CI company and their respective Subsidiaries taken together, comprise all of the companies through which all of the American Apparel business or similar or related apparel businesses that are owned and operated jointly by the Stockholder and Lim, including all designing, marketing, branding, manufacturing, distribution and retail store operations in the U.S. and abroad, is operated.

(b) The Company is duly qualified or licensed to do business as a foreign corporation and is in good standing in each jurisdiction where the character of the properties owned, leased or operated by it or the nature of its activities makes such qualification or licensing necessary, except for such failures to be so duly qualified or licensed and in good standing that could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on the Company. Each jurisdiction in which the Company is so qualified or licensed is listed in *Schedule 2.1(b)*.

(c) The minute books of each of AAI, each CI company and LLC contain true, complete and accurate records of all meetings and consents in lieu of meetings of its Board of Directors (and any committees thereof), similar governing bodies and stockholders and members (*Corporate Records*) since the time of their respective organization. Copies of such Corporate Records have been heretofore delivered to Parent or Parent s counsel.

(d) The stock/equity transfer, warrant and option transfer and ownership records of each of AAI, each CI company and LLC contain true, complete and accurate records of the securities ownership as of the date of such records and the transfers involving the capital stock, equity interests and other securities of such company since the time of its organization. Copies of such records have been heretofore delivered to Parent or Parent s counsel.

(e) AAI is a duly qualified S Corporation within the meaning of Section 1361 et seq. of the Internal Revenue Code of 1986, as amended. A valid election under IRC § 1362(a) to be treated as an S corporation is in effect for AAI. Other than in connection with the transactions contemplated hereby, no action has been taken by any shareholder of AAI or AAI to terminate AAI s status as an S corporation.

2.2 *Subsidiaries*.

(a) The Company does not have any direct or indirect subsidiaries or participations in joint ventures other than those listed in *Schedule 2.2* (the *Subsidiaries*). Except as set forth in Schedule 2.2, the Company does not own all of the outstanding equity securities of its respective Subsidiaries, free and clear of all Liens (as defined in Section 10.2(e)). Except for the Subsidiaries, the Company does not own, directly or indirectly, any ownership, equity, profits or voting interest in any Person or has any agreement or commitment to purchase any such interest, and has not agreed and is not obligated to make nor is bound by any written, oral or other agreement, contract, subcontract, lease, binding understanding, instrument, note, option, warranty, purchase order, license, sublicense, insurance policy, benefit plan, commitment or undertaking of any nature, as of the date hereof or as may hereafter be in effect under which it may become obligated to make, any future investment in or capital contribution to any other entity.

(b) Each Subsidiary that is a corporation or limited liability company is duly incorporated or organized, as the case may be, validly existing and in good standing under the laws of its state of incorporation or organization (as listed in *Schedule 2.2*) and has the requisite corporate or limited liability company power and authority to own, lease and operate its assets and properties and to carry on its business as it is now being or currently planned by the Company to be conducted. Each Subsidiary is in possession of all Approvals necessary to own, lease and operate the properties it purports to own, operate or lease and to carry on its business as it is now being or currently planned by the Company to be conducted, except where the failure to have such Approvals could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on the Company or such Subsidiary. Complete and correct copies of the

Charter Documents of each Subsidiary, as amended and currently in effect, have been heretofore delivered to Parent or Parent s counsel. No Subsidiary is in violation of any of the provisions of its Charter Documents.

(c) Each Subsidiary is duly qualified or licensed to do business as a foreign corporation or foreign limited liability company and is in good standing in each jurisdiction where the character of the properties owned, leased or operated by it or the nature of its activities makes such qualification or licensing necessary, except for such failures to be so duly qualified or licensed and in good standing that could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on the Company or such Subsidiary. Each jurisdiction in which each Subsidiary is so qualified or licensed is listed in *Schedule 2.2.*

(d) The minute books of each Subsidiary contain true, complete and accurate records of all meetings and consents in lieu of meetings of its board of directors (and any committees thereof), similar governing bodies and stockholders or membership interest holders since its formation. Copies of the Corporate Records of each Subsidiary have been heretofore been delivered to Parent or Parent s counsel.

2.3 *Capitalization.*

(a) The authorized capital stock of AAI consists of 1,000,000 shares of common stock, of which 100,000 shares are issued and outstanding as of the date of this Agreement, all of which are validly issued, fully paid and nonassessable and are owned by the Stockholder and Lim in the respective amounts set forth on *Schedule 2.3(a)* hereto. All of such capital stock of AAI is owned by such Persons free and clear of any Liens (as defined) and, giving effect to the Stockholders Agreements Waivers as defined and provided for under Section 5.11(b) of this Agreement, such Person has all right (including under applicable laws governing marital property) to sell and transfer such capital stock as contemplated by this Agreement and upon such sale and transfer, such capital stock shall be acquired by Merger Sub free and clear of any Liens.

(b) The authorized capital stock of each CI company is as set forth on *Schedule 2.3(b)*. All of the outstanding shares of capital stock of each CI company are validly issued, fully paid and nonassessable and are owned by the Persons who are indicated as CI Stockholders on *Schedule 2.3(b)* hereto in the respective amounts set forth on *Schedule 2.3(b)* hereto. All of such capital stock of each CI company is owned by each such Person free and clear of any Liens and, giving effect to the Stockholders Agreements Waivers, such Person has all right (including under applicable laws governing marital property) to transfer such capital stock as contemplated by this Agreement and upon such transfer, such capital stock of each CI company shall be acquired by Parent free and clear of any Liens. The Stockholder is the ultimate owner of all outstanding shares of capital stock of each of the CI companies either directly or through nominees and has sole right and title to all such capital stock and to vote such capital stock and has the authority, power and capacity to cause his nominees to comply with the terms of this Agreement and the transactions contemplated hereby.

(c) The authorized capitalization of LLC consists of one class of membership interests, 50% of which are owned by the Stockholder and 50% of which are owned by Lim. All of LLC s membership interests are validly issued, fully paid and nonassessable. All of such membership interests are owned by each such Person free and clear of any Liens and, giving effect to the Stockholders Agreements Waivers, such Person has all right (including under applicable laws governing marital property) to sell and transfer such membership interests as contemplated by this Agreement and upon such sale and transfer, such membership interest shall be acquired by AAI as contemplated by Section 5.26 of this Agreement free and clear of any Liens.

(d) As of the date of this Agreement, (i) no shares of Company Capital Stock or any membership interests of LLC or any Subsidiary (*Company Membership Interests*) are reserved for issuance upon the exercise of outstanding options granted to any person (*Company Stock Options*), and (ii) no shares of Company Capital Stock or Company Membership Interests are reserved for issuance upon the exercise of outstanding warrants or other rights (*Company Warrants*). There are no commitments or agreements of any character to which the Company is bound obligating the Company to accelerate the vesting of any Company Stock Option or Company Warrant as a result of the Business Combination.

Table of Contents

(e) All outstanding shares of Company Capital Stock and all Company Membership Interests have been issued in compliance with (x) all applicable securities laws and (in all material respects) other applicable laws and regulations, and (y) all requirements set forth in any applicable Company Contracts (as defined in Section 2.19).

(f) Giving effect to the Stockholders Agreements Waivers, there are no subscriptions, options, warrants, equity securities, partnership interests or similar ownership interests, calls, rights (including preemptive rights), commitments or agreements of any character to which the Company is a party or by which it is bound obligating the Company to issue, deliver or sell, or cause to be issued, delivered or sold, or repurchase, redeem or otherwise acquire, or cause the repurchase, redemption or acquisition of, any shares of capital stock or similar ownership interests of the Company or any Subsidiary or obligating the Company to grant, extend, accelerate the vesting of or enter into any such subscription, option, warrant, equity security, call, right, commitment or agreement.

(g) Except as contemplated by this Agreement, there are no registration rights, and there is no voting trust, proxy, rights plan, antitakeover plan or other agreement or understanding to which the Company is a party or by which the Company is bound with respect to any equity security of any class of the Company.

(h) Giving effect to the Stockholders Agreement waivers, no outstanding shares of Company Capital Stock or Company Membership Interests are unvested or are subject to a repurchase option, risk of forfeiture or other condition under any applicable agreement with the Company.

(i) The authorized and outstanding capital stock of each Subsidiary is as set forth in *Schedule 2.3(i)* hereto. Except as set forth in *Schedule 2.3(i)*, the Company owns all of the outstanding equity securities and membership interests of each Subsidiary, free and clear of all Liens, either directly or indirectly through one or more other Subsidiaries. There are no outstanding options, warrants or other rights to purchase securities or membership interests of any Subsidiary.

2.4 *Authority Relative to this Agreement*.

(a) Giving effect to the Stockholders Agreement Waivers, AAI, each CI company, LLC, the Stockholder, each of the CI Stockholders and Lim has all necessary power and authority to execute and deliver this Agreement and to perform its, his or her obligations hereunder and to consummate the transactions contemplated hereby (including the Business Combination).

(b) The execution and delivery of this Agreement and the consummation by each of AAI, each CI company and LLC of the transactions contemplated hereby (including the Business Combination) have been duly and validly authorized by all necessary corporate or limited liability company action on the part of each of AAI, each CI company and LLC (including the approval by its board of directors, managers, members and stockholders, subject in all cases to the satisfaction of the terms and conditions of this Agreement, including the conditions set forth in Article VI), and no other corporate or limited liability company proceedings on the part of the Company or its stockholders or members are necessary to authorize this Agreement or to consummate the transactions contemplated hereby pursuant to the Applicable Corporate Laws and the terms and conditions of this Agreement.

(c) This Agreement has been duly and validly executed and delivered by each of AAI, each CI company, LLC, the Stockholder and each of the CI Stockholders, and assuming the due authorization, execution and delivery thereof by the other parties hereto, constitutes the legal and binding obligation of each such Person, enforceable against each such Person in accordance with its terms, except as may be limited by bankruptcy, insolvency, reorganization or other similar laws affecting the enforcement of creditors rights generally and by general principles of equity.

(d) This Agreement has been duly and validly executed and delivered by Lim and, assuming the due authorization, execution and delivery thereof by the other parties hereto, constitutes the legal and binding obligation of Lim, enforceable against him in accordance with its terms, except as may be limited by bankruptcy, insolvency, reorganization or other similar laws affecting the enforcement of creditors rights generally and by general principles of equity.

Table of Contents

2.5 *No Conflict; Required Filings and Consents*.

(a) The execution and delivery of this Agreement by each of AAI, each CI Company, LLC, the Stockholder, the CI Stockholders and Lim do not, and the performance of this Agreement by such Persons shall not, (i) conflict with or violate the Company s Charter Documents, (ii) conflict with or violate any Legal Requirements (as defined in Section 10.2(c)), (iii) result in any breach of or constitute a default (or an event that with notice or lapse of time or both would become a default) under, or materially impair the Company s rights or alter the rights or obligations of any third party under, or give to others any rights of termination, amendment, acceleration or cancellation of, or result in the creation of a lien or encumbrance on any of the properties or assets of the Company pursuant to, any Company Contracts, or (iv) result in the triggering, acceleration or increase of any payment to any Person pursuant to any Company Contract, including any change in control or similar provision of any Company Contract, except, with respect to clauses (ii), (iii) or (iv), for any such conflicts, violations, breaches, defaults, triggerings, accelerations, increases or other occurrences that would not, individually and in the aggregate, have a Material Adverse Effect on the Company.

(b) The execution and delivery of this Agreement by each of AAI, each CI Company, LLC the Stockholder, the CI Stockholders and Lim does not, and the performance of its, his or her obligations hereunder will not, require any consent, approval, authorization or permit of, or filing with or notification to, any Governmental Entity or other third party (including, without limitation, lenders and lessors, except (i) for applicable requirements, if any, of the Securities Act, the Exchange Act or Blue Sky Laws, and the rules and regulations thereunder, and appropriate documents received from or filed with the relevant authorities of other jurisdictions in which the Company is licensed or qualified to do business, (ii) for the filing of any notifications required under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (the *HSR Act*), and, if applicable, the Competition Act (Canada) and Investment Canada Act (together, the *Canada Acts*) and the expiration of the required waiting periods thereunder, (iii) the consents, approvals, authorizations and permits described in *Schedule 2.5(b)* hereto, (iv) for the application with the Canada Revenue Agency for the Section 116 Certificate, and (v) where the failure to obtain such consents, approvals, authorizations or permits, or to make such filings or notifications, would not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on the Company or, after the Closing, Parent, U.S. Surviving Corporation or the CI companies or prevent consummation of the Business Combination or otherwise prevent the parties hereto from performing their obligations under this Agreement.

2.6 *Compliance*. The Company has complied with and is not in violation of any Legal Requirements with respect to the conduct of its business, or the ownership or operation of its business, except for failures to comply or violations which, individually or in the aggregate, have not had and are not reasonably likely to have a Material Adverse Effect on the Company. Except as set forth in *Schedule 2.6*, no written notice of non-compliance with any Legal Requirements has been received by the Company (and the Company has no knowledge of any such notice delivered to any other Person). The Company is not in violation of any term of any Company Contract, except for failures to comply or violations which, individually or in the aggregate, have not had and are not reasonably likely to have a Material Adverse Effect on the Company.

2.7 *Financial Statements*.

(a) AAI has provided to Parent audited consolidated financial statements (including any related notes thereto) for the fiscal year ended June 30, 2004, the transition six month period ended December 31, 2004 and draft consolidated financial statements (including any related notes thereto) for the fiscal year ended December 31, 2005 and CI has provided to Parent audited combined financial statements for the fiscal years ended December 31, 2004 and 2005 (collectively, the *Annual Financial Statements*). The Annual Financial Statements were prepared in accordance with the published rules and regulations of any applicable Governmental Entity and with generally accepted accounting principles of the United States (*U.S. GAAP*) or Canada (*Canada GAAP*), as applicable, applied on a consistent basis throughout the periods involved

(except as may be indicated in the notes thereto) and each fairly presents in all material respects the financial position of the applicable companies at the respective dates thereof and the results of its operations and cash flows for the periods indicated.

(b) AAI has provided to Parent a correct and complete copy of the unaudited consolidated financial statements (including any related notes thereto) of AAI for the ten-month period ended October 31, 2006 and CI has provided to Parent a correct and complete copy of the unaudited combined financial statement (including, any notes thereto) of CI for the ten-month period ended October 31, 2006 (collectively, the *Stub Financial Statements*). The Stub Financial Statements comply as to form in all material respects, and were prepared in accordance, with the published rules and regulations of any applicable Governmental Entity and with U.S. GAAP or Canada GAAP, as applicable, applied on a consistent basis throughout the periods involved (except as may be indicated in the notes thereto), are consistent with the Annual Financial Statements and fairly present in all material respects the financial position of the applicable companies at the date thereof and the results of its operations and cash flows for the period indicated, except that such statements do not contain notes and are subject to normal audit adjustments.

(c) The books of account, minute books, stock certificate books and stock transfer ledgers and other similar books and records of the Company have been maintained in accordance with good business practice, are complete and correct in all material respects and there have been no material transactions that are required to be set forth therein and which have not been so set forth.

(d) The accounts and notes receivable of the Company reflected on the balance sheets included in the Annual Financial Statements and the Stub Financial Statements (i) arose from bona fide sales transactions in the ordinary course of business and are payable on ordinary trade terms, (ii) are legal, valid and binding obligations of the respective debtors enforceable in accordance with their terms, except as such may be limited by bankruptcy, insolvency, reorganization, or other similar laws affecting creditors rights generally, and by general equitable principles, (iii) are not subject to any valid set-off or counterclaim except to the extent set forth in such balance sheet contained therein, (iv) are collectible in the ordinary course of business consistent with past practice in the aggregate recorded amounts thereof, net of any applicable reserve reflected in such balance sheet referenced above, and (v) are not the subject of any actions or proceedings brought by or on behalf of the Company. All inventory reflected on the Annual Financial Statements and the Stub Financial Statements were produced in the ordinary course of business consistent with past practice and represents saleable goods.

(e) LLC has not conducted any operations since January 1, 2004 and has not had any revenues, expenses or losses since such date and has no obligations to any party, whether now owing or which would become owed given the passage of time, except as set forth on *Schedule 2.7(e)*, and has not been audited and has not produced financial statements (nor has it been required to under law or contract) since such date. LLC is not a party to any Company Contract (as defined). LLC has no assets or liabilities.

2.8 *No Undisclosed Liabilities*. Except as set forth in *Schedule 2.8* hereto, the Company has no liabilities (absolute, accrued, contingent or otherwise) of a nature required to be disclosed on a balance sheet or in the related notes to financial statements that are, individually or in the aggregate, material to the business, results of operations or financial condition of the Company, except: (i) liabilities provided for in or otherwise disclosed in the interim balance sheet included in the Stub Financial Statements or in the notes to the Annual Financial Statements, and (ii) such liabilities arising in the ordinary course of the Company s business since January 1, 2006, none of which would have a Material Adverse Effect on the Company.

2.9 *Absence of Certain Changes or Events*. Except as set forth in *Schedule 2.9* hereto or in the Stub Financial Statements, since January 1, 2006, there has not been: (i) any Material Adverse Effect on the Company, (ii) any declaration, setting aside or payment of any dividend on, or other distribution (whether in cash, stock or property) in respect of, any of the Company s stock, or any purchase, redemption or other acquisition by the Company of any of the Company s capital stock or any other securities of the Company or any options, warrants, calls or rights to acquire any such shares or other securities, (iii) any split, combination or reclassification of any

Table of Contents

of the Company s capital stock, (iv) any granting by the Company of any increase in compensation or fringe benefits, except for normal increases of cash compensation in the ordinary course of business consistent with past practice, or any payment by the Company of any bonus, except for bonuses made in the ordinary course of business consistent with past practice, or any granting by the Company of any increase in severance or termination pay or any entry by the Company into any currently effective employment, severance, termination or indemnification agreement or any agreement the benefits of which are contingent or the terms of which are materially altered upon the occurrence of a transaction involving the Company of the nature contemplated hereby, (v) entry by the Company into any licensing or other agreement with regard to the acquisition or disposition of any Intellectual Property (as defined in Section 2.18 hereof) other than licenses in the ordinary course of business consistent with past practice or any amendment or consent with respect to any licensing agreement filed or required to be filed by the Company with respect to any Governmental Entity, (vi) any material change by the Company in its accounting methods, principles or practices, (vii) any change in the auditors of the Company, (viii) any issuance of capital stock of the Company, (ix) any revaluation by the Company of any of its assets, including, without limitation, writing down the value of capitalized inventory or writing off notes or accounts receivable or any sale of assets of the Company other than in the ordinary course of business, or (x) any agreement, whether written or oral, to do any of the foregoing.

2.10 *Litigation*.

(a) *Schedule 2.10(a)* sets forth all claims, suits, actions or proceedings pending or, to the knowledge of the Company, threatened against the Company or any director or officer thereof before any court, government department, commission, agency, instrumentality or authority, or any arbitrator.

(b) Except as disclosed in *Schedule 2.10(b)* hereto, there are no claims, suits, actions or proceedings pending or, to the knowledge of the Company, threatened against the Company, the Stockholder, any of the CI Stockholders or Lim before any court, governmental department, commission, agency, instrumentality or authority, or any arbitrator that seeks to restrain or enjoin the consummation of the transactions contemplated by this Agreement or which could reasonably be expected, either singularly or in the aggregate with all such claims, actions or proceedings, to have a Material Adverse Effect on the Company or have a Material Adverse Effect on the ability of the parties hereto to consummate the Business Combination.

2.11 *Employee Benefit Plans*.

(a) *Schedule 2.11(a)* lists all employee compensation, incentive, fringe or benefit plans, programs, policies, commitments or other arrangements (whether or not set forth in a written document) covering any active or former employee, director or consultant of the Company, or any trade or business (whether or not incorporated) which is under common control with the Company, with respect to which the Company has liability (individually, a *Plan* and, collectively, the *Plans*). All Plans have been maintained and administered in all material respects in compliance with their respective terms and with the requirements prescribed by any and all statutes, orders, rules and regulations which are applicable to such Plans, and all liabilities with respect to the Plans have been properly reflected in the financial statements and records of the Company. No suit, action or other litigation (excluding claims for benefits incurred in the ordinary course of Plan activities) has been brought, or, to the knowledge of the Company, is threatened, against or with respect to any Plan. There are no audits, inquiries or proceedings pending or, to the knowledge of the Company, threatened by any governmental agency with respect to any Plan. All contributions, reserves or premium payments required to be made or accrued as of the date hereof to the Plans have been timely made or accrued. The Company does not have any plan or commitment to establish any new Plan, to modify any Plan (except to the extent required by law or to conform any such Plan to the requirements of any applicable law, in each case as previously disclosed to Parent in writing, or as required by this Agreement), or to enter into any new Plan. Each Plan can be amended, terminated or otherwise discontinued after the Closing in accordance with its terms, without liability to Parent or the Company (other than ordinary administration expenses and expenses for benefits accrued but not yet paid).

(b) Except as disclosed in *Schedule* 2.11(b) hereto, neither the execution and delivery of this Agreement nor the consummation of the transactions contemplated hereby will (i) result in any payment (including severance, unemployment compensation, golden parachute, bonus or otherwise) becoming due to any stockholder, director or employee of the Company under any Plan or otherwise, (ii) materially increase any benefits otherwise payable under any Plan, or (iii) result in the acceleration of the time of payment or vesting of any such benefits.

2.12 *Labor Matters*. The Company is not a party to any collective bargaining agreement or other labor union contract applicable to persons employed by the Company and the Company does not know of any activities or proceedings of any labor union to organize any such employees. Any action, complaint or investigation brought against the Company by the National Labor Relations Board or any other federal, foreign, state, provincial or local government or agency or administrative body since inception of any of AAI or any CI company is listed on *Schedule 2.12* hereto.

2.13 *Restrictions on Business Activities*. Except as disclosed in *Schedule 2.13* hereto, to the Company s knowledge, there is no agreement, commitment, judgment, injunction, order or decree binding upon the Company or its assets or to which the Company is a party which has or could reasonably be expected to have the effect of prohibiting or materially impairing any business practice of the Company, any acquisition of property by the Company or the conduct of business by the Company as currently conducted other than such effects, individually or in the aggregate, which have not had and would not reasonably be expected to have a Material Adverse Effect on the Company.

2.14 *Title to Property*.

(a) All real property owned by the Company (including improvements and fixtures thereon, easements and rights of way) is shown or reflected on the balance sheet of the Company included in the Stub Financial Statements. The Company has good, valid and marketable fee simple title to the real property owned by it, and except as set forth in the Stub Financial Statements or on *Schedule 2.14(a)* hereto, all of such real property is held free and clear of (i) all leases, licenses and other rights to occupy or use such real property and (ii) all Liens, rights of way, easements, restrictions, exceptions, variances, reservations, covenants or other title defects or limitations of any kind, other than liens for taxes not yet due and payable and such liens or other imperfections of title, if any, as do not materially detract from the value of or materially interfere with the present use of the property affected thereby. *Schedule 2.14(a)* hereto also contains a list of all options or other contracts under which the Company has a right to acquire any interest in real property.

(b) All leases of real property held by the Company, and all personal property and other property and assets of the Company owned, used or held for use in connection with the business of the Company (the *Personal Property*) are shown or reflected on the balance sheet included in the Annual Financial Statements, other than those entered into or acquired on or after January 1, 2006 in the ordinary course of business. The Company has good and marketable title to the Personal Property owned by it, and all such Personal Property is in each case held free and clear of all Liens, except for Liens disclosed in the Annual Financial Statements or in *Schedule 2.14* hereto, none of which liens or encumbrances has or will have, individually or in the aggregate, a Material Adverse Effect on such property or on the present or contemplated use of such property in the businesses of the Company.

(c) All leases pursuant to which the Company leases from others material real or Personal Property are valid and effective in accordance with their respective terms, and there is not, under any of such leases, any existing material default or event of default of the Company or, to the Company s knowledge, any other party (or any event which with notice or lapse of time, or both, would constitute a material default), except where the lack of such validity and effectiveness or the existence of such default or event of default could not reasonably be expected to have a Material Adverse Effect on the Company.

(d) The Company is in possession of, or has valid and effective rights to, all properties, assets and rights (including Intellectual Property) required for the conduct of its business in the ordinary course.

Table of Contents

2.15 *Taxes*.

(a) *Definition of Taxes.* For the purposes of this Agreement, *Tax* or *Taxes* refers to any and all federal, foreign, state, provincial, local and foreign taxes, including, without limitation, gross receipts, income, profits, sales, use, occupation, value added, ad valorem, transfer, franchise, withholding, payroll, recapture, employment, excise and property taxes, assessments, governmental charges and duties together with all interest, penalties and additions imposed with respect to any such amounts and any obligations under any agreements or arrangements with any other Person with respect to any such amounts and including any liability of a predecessor entity for any such amounts.

(b) *Tax Returns and Audits.* Except as set forth in *Schedule 2.15* hereto:

(i) The Company has timely filed all federal, state, local and foreign returns, estimates, information statements and reports relating to Taxes (*Returns*) required to be filed by the with any Tax authority prior to the date hereof, except such Returns which are not material to the Company. All such Returns are true, correct and complete in all material respects. The Company has paid all Taxes shown to be due and payable on such Returns. Each member of the LLC and each stockholder of AAI have filed individual Returns as and when required with respect to their ownership of LLC and AAI and has paid all Taxes shown to be due and payable on such Returns.

(ii) All Taxes that the Company is required by law to withhold or collect have been duly withheld or collected, and have been timely paid over to the proper governmental authorities to the extent due and payable.

(iii) The Company (or in the case of LLC or AAI, any LLC member or AAI stockholder) has not been delinquent in the payment of any material Tax nor is there any material Tax deficiency outstanding, proposed or assessed against the Company (or such person), nor has the Company (or any such person) executed any unexpired waiver of any statute of limitations on or extending the period for the assessment or collection of any Tax.

(iv) To the knowledge of the Company and the Stockholder, no audit or other examination of any Return of the Company (or any LLC member or AAI stockholder) by any Tax authority is presently in progress, nor has the Company or the Stockholder been notified of any request for such an audit or other examination.

(v) No adjustment relating to any Returns filed by the Company (or any LLC member or AAI stockholder) has been proposed in writing, formally or informally, by any Tax authority to the Company or any representative thereof.

(vi) The Company has no liability for any material unpaid Taxes which have not been accrued for or reserved on the Company s balance sheets included in the Annual Financial Statements or the Stub Financial Statements, whether asserted or unasserted, contingent or otherwise, which is material to the Company, other than any liability for unpaid Taxes that may have accrued since the end of the most recent fiscal year in connection with the operation of the business of the Company in the ordinary course of business, none of which is material to the business, results of operations or financial condition of the Company.

(vii) Neither the Company nor the Stockholder has taken any action and does not know of any fact, agreement, plan or other circumstance that is reasonably likely to prevent the Merger and each Canada Acquisition from qualifying as a reorganization within the meaning of Section 368(a) of the Code.

(viii) No transaction or arrangement between a CI company and any person with whom the CI company was not dealing at arm s length within the meaning of the *Income Tax Act* (Canada) involving the acquisition, delivery, disposition or provision of property or services or the right to use property or services, took place for consideration that is other than the fair market value for such property, services or right and such transaction or arrangement was made on arm s length terms and conditions. Each CI

company has made or obtained records or documents that meet the requirements of paragraphs 247(4)(a) to (c) of the *Income Tax Act* (Canada) with respect to all transactions and arrangements between such CI company and any non-resident person, within the meaning of the *Income Tax Act* (Canada), with whom such CI company was not dealing at arm s length, within the meaning of the *Income Tax Act* (Canada).

(ix) None of the CI companies is subject to a liability for Taxes of any other person, including without limitation, liability arising under section 160 of the *Income Tax Act* (Canada). None of the CI companies has (a) made any payment, (b) is obligated to make any payment, or (c) is a party to any agreement under which it could be obligated to make any payment, that will not be deductible in computing its income under the *Income Tax Act* (Canada) by virtue of section 67 of the *Income Tax Act* (Canada).

2.16 *Environmental Matters*.

(a) Except as disclosed in *Schedule 2.16* hereto and except for such matters that, individually or in the aggregate, are not reasonably likely to have a Material Adverse Effect: (i) the Company has complied with all applicable Environmental Laws (as defined below); (ii) the properties currently operated by the Company (including soils, groundwater, surface water, air, buildings or other structures) are not contaminated with any Hazardous Substances (as defined below); (iii) the properties formerly owned or operated by the Company were not contaminated with Hazardous Substances during the period of ownership or operation by the Company or, to the Company s knowledge, during any prior period; (iv) the Company is not subject to liability for any Hazardous Substance disposal or contamination on any third party or public property (whether above, on or below ground or in the atmosphere or water); (v) the Company has not been associated with any release or threat of release of any Hazardous Substance; (vi) the Company has not received any notice, demand, letter, claim or request for information alleging that the Company may be in violation of or liable under any Environmental Law; and (vii) the Company is not subject to any orders, decrees, injunctions or other arrangements with any Governmental Entity or subject to any indemnity or other agreement with any third party relating to liability under any Environmental Law or relating to Hazardous Substances.

(b) As used in this Agreement, the term *Environmental Law* means any federal, foreign, state, provincial, local or foreign law, regulation, order, decree, permit, authorization, opinion, common law or agency requirement relating to: (A) the protection, investigation or restoration of the environment, health and safety, or natural resources; (B) the handling, use, presence, disposal, release or threatened release of any Hazardous Substance or (C) noise, odor, wetlands, pollution, contamination or any injury or threat of injury to persons or property.

(c) As used in this Agreement, the term *Hazardous Substance* means any substance that is: (i) listed, classified or regulated pursuant to any Environmental Law; (ii) any petroleum product or by-product, asbestos-containing material, lead-containing paint or plumbing, polychlorinated biphenyls, radioactive materials or radon; or (iii) any other substance which is the subject of regulatory action by any Governmental Entity pursuant to any Environmental Law.

(d) *Schedule 2.16(d)* sets forth all environmental studies and investigations completed or in process with respect to the Company and/or its subsidiaries or their respective properties or assets, including all phase reports, that are known to the Company. All such written reports and material documentation relating to any such study or investigation has been provided by the Company to Parent.

2.17 *Brokers; Third Party Expenses*. The Company has not incurred, nor will it incur, directly or indirectly, any liability for brokerage, finders fees, agent s commissions or any similar charges in connection with this Agreement or any transactions contemplated hereby. Except as disclosed in *Schedule 2.17* hereto, no shares of common stock, options, warrants or other securities of either the Company or Parent are payable by the Company, the Stockholder, the CI Stockholders or Lim to any third party by the Company as a result of the Business Combination.

Table of Contents

2.18 *Intellectual Property*.

(a) *Schedule 2.18* hereto contains a description of all material Intellectual Property of the Company. For the purposes of this Agreement, the following terms have the following definitions:

Intellectual Property shall mean any or all of the following and all worldwide common law and statutory rights in, arising out of, or associated therewith: (i) patents and applications therefor and all reissues, divisions, renewals, extensions, provisionals, continuations and continuations-in-part thereof (*Patents*); (ii) inventions (whether patentable or not), invention disclosures, improvements, trade secrets, proprietary information, know how, technology, technical data and customer lists, and all documentation relating to any of the foregoing; (iii) copyrights, copyrights registrations and applications therefor, and all other rights corresponding thereto throughout the world (*Copyrights*); (iv) software and software programs; (v) domain names, uniform resource locators and other names and locators associated with the Internet (vi) industrial designs and any registrations and applications therefor; (vii) trade names, logos, common law trademarks and service marks, trademark and service mark registrations and applications therefor (collectively, *Trademarks*); (viii) all databases and data collections and all rights therein; (ix) all moral and economic rights of authors and inventors, however denominated, and (x) any similar or equivalent rights to any of the foregoing (as applicable).

Company Intellectual Property shall mean any Intellectual Property that is owned by, or exclusively licensed to, the Company, including software and software programs developed by or exclusively licensed to the Company (specifically excluding any off the shelf or shrink-wrap software).

Registered Intellectual Property means all Intellectual Property that is the subject of an application, certificate, filing, registration or other document issued, filed with, or recorded by any government or other legal authority.

Company Registered Intellectual Property means all of the Registered Intellectual Property owned by, or filed in the name of, the Company.

Company Products means all current versions of products or service offerings of the Company.

(b) Except as disclosed in *Schedule* 2.18 hereto, no Company Intellectual Property or Company Product is subject to any material proceeding or outstanding decree, order, judgment, contract, license or stipulation restricting in any manner the use, transfer or licensing thereof by the Company, or which may affect the validity, use or enforceability of such Company Intellectual Property or Company Product, which in any such case could reasonably be expected to have a Material Adverse Effect on the Company.

(c) The Company owns or has enforceable rights to use all Intellectual Property required for the conduct of its business as presently conducted or as presently contemplated to be conducted. Except as disclosed in *Schedule 2.18* hereto, the Company owns and has good and exclusive title to each material item of Company Intellectual Property owned by it free and clear of any Liens (excluding non-exclusive licenses and related restrictions granted by it in the ordinary course of business); and the Company is the exclusive owner of all material registered Trademarks and Copyrights used in connection with the operation or conduct of the business of the Company including the sale of any products or the provision of any services by the Company.

(d) The operation of the business of the Company as such business currently is conducted, including the Company s use of any product, device or process, has not and does not infringe or misappropriate the Intellectual Property of any third party or constitute unfair competition or trade practices under the laws of any jurisdiction and the Company has not received any claims or threats from third parties alleging any such infringement, misappropriation or unfair competition or trade practices.

Table of Contents

2.19 *Agreements, Contracts and Commitments*.

(a) *Schedule 2.19(a)* hereto sets forth a complete and accurate list of all Material Company Contracts (as hereinafter defined), specifying the parties thereto. For purposes of this Agreement, (i) the term *Company Contracts* shall mean all contracts, agreements, leases, mortgages, indentures, notes, bonds, licenses, permits, franchises, purchase orders, sales orders, and other understandings, commitments and obligations (including without limitation outstanding offers and proposals) of any kind, whether written or oral, to which the Company is a party or by or to which any of the properties or assets of the Company may be bound, subject or affected (including without limitation notes or other instruments payable to the Company) and (ii) the term *Material Company Contracts* shall mean (x) each Company Contract (I) providing for payments (present or future) to the Company in excess of $50,000 in the aggregate or (II) under which or in respect of which the Company presently has any liability or obligation of any nature whatsoever (absolute, contingent or otherwise) in excess of $50,000, (y) each Company Contract that otherwise is or may be material to the businesses, operations, assets, condition (financial or otherwise) or prospects of the Company and (z) without limitation of subclause (x) or subclause (y), each of the following Company Contracts:

(i) any mortgage, indenture, note, installment obligation or other instrument, agreement or arrangement for or relating to any borrowing of money from the Company by any officer, director, stockholder or holder of derivative securities of the Company (each such person, an *Insider*);

(ii) any mortgage, indenture, note, installment obligation or other instrument, agreement or arrangement for or relating to any borrowing of money from an Insider by the Company;

(iii) any guaranty, direct or indirect, by the Company, a Subsidiary or any Insider of the Company of any obligation for borrowings, or otherwise, excluding endorsements made for collection in the ordinary course of business;

(iv) any Company Contract of employment or management;

(v) any Company Contract made other than in the ordinary course of business or (x) providing for the grant of any preferential rights to purchase or lease any asset of the Company or (y) providing for any right (exclusive or non-exclusive) to sell or distribute, or otherwise relating to the sale or distribution of, any product or service of the Company;

(vi) any obligation to register any shares of the capital stock or other securities of the Company with any Governmental Entity;

(vii) any obligation to make payments, contingent or otherwise, arising out of the prior acquisition of the business, assets or stock of other Persons;

(viii) any collective bargaining agreement with any labor union;

(ix) any lease or similar arrangement for the use by the Company of real property or personal property (other than any lease of vehicles, office equipment or operating equipment made in the ordinary course of business where the annual lease payments are less than $25,000);

(x) any Company Contract granting or purporting to grant, or otherwise in any way relating to, any mineral rights or any other interest (including, without limitation, a leasehold interest) in real property;

(xi) any Company Contract to which any Insider of the Company is a party; and

(xii) any offer or proposal which, if accepted, would constitute any of the foregoing.

(b) Each Material Company Contract was entered into at arms length and in the ordinary course, is in full force and effect and, to the Company s knowledge, is valid and binding upon and enforceable against each of the parties thereto (except insofar as enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors rights generally or by principles governing the availability of equitable remedies), except where same has not had and would not reasonably be expected to have a Material Adverse Effect. To the knowledge of the Company, no other party to a

Table of Contents

Material Company Contract is the subject of a bankruptcy or insolvency proceeding. True, correct and complete copies of all Material Company Contracts and offers and proposals, which, if accepted, would constitute Material Company Contracts (or written summaries in the case of oral Material Company Contracts or oral offers and proposals, which if accepted, would constitute Material Company Contracts), and of all outstanding offers and proposals of the Company have been heretofore delivered to Parent or Parent s counsel.

(c) Except as set forth in *Schedule 2.19(c)*, neither the Company nor, to the best of the Company s knowledge, any other party thereto is in breach of or in default under, and no event has occurred which with notice or lapse of time or both would become a breach of or default under, any Company Contract, and no party to any Company Contract has given any written notice of any claim of any such breach, default or event, which, individually or in the aggregate, are reasonably likely to have a Material Adverse Effect on the Company. Each Material Company Contract to which the Company is a party or by which it is bound that has not expired by its terms is in full force and effect.

2.20 *Insurance*. *Schedule 2.20* sets forth the Company s insurance policies and fidelity bonds covering the assets, business, equipment, properties, operations, employees, officers and directors (collectively, the *Insurance Policies*). The insurances provided by such Insurance Policies are adequate in amount and scope for the Company s business and operations, including any insurance required to be maintained by Company Contracts.

2.21 *Governmental Actions/Filings*.

(a) Except as set forth in *Schedule 2.21(a)*, the Company has been granted and holds, and has made, all Governmental Actions/Filings (as defined below) (including, without limitation, the Governmental Actions/Filings required for (i) emission or discharge of effluents and pollutants into the air and the water and (ii) the manufacture and sale of all products manufactured and sold by it) necessary to the conduct by the Company of its business (as presently conducted and as presently proposed to be conducted) or used or held for use by the Company, and true, complete and correct copies of which have heretofore been delivered to Parent. Each such Governmental Action/Filing is in full force and effect and, except as disclosed in *Schedule 2.21(a)* hereto, will not expire prior to December 31, 2008, and the Company is in compliance with all of its obligations with respect thereto. No event has occurred and is continuing which requires or permits, or after notice or lapse of time or both would require or permit, and consummation of the transactions contemplated by this Agreement or any ancillary documents will not require or permit (with or without notice or lapse of time, or both), any modification or termination of any such Governmental Actions/Filings except such events which, either individually or in the aggregate, would not have a Material Adverse Effect upon the Company.

(b) Except as set forth in *Schedule 2.21(b)*, no Governmental Action/Filing is necessary to be obtained, secured or made by the Company to enable it to continue to conduct its businesses and operations and use its properties after the Closing in a manner which is consistent with current practice.

(c) For purposes of this Agreement, the term *Governmental Action/Filing* shall mean any franchise, license, certificate of compliance, authorization, consent, order, permit, approval, consent or other action of, or any filing, registration or qualification with, any federal, foreign, state, provincial, municipal, foreign or other governmental, administrative or judicial body, agency or authority.

2.22 *Interested Party Transactions*.

(a) Except as set forth in the *Schedule 2.22* hereto, no employee, officer, director or stockholder of the Company or a member of his or her immediate family is indebted to the Company, nor is the Company indebted (or committed to make loans or extend or guarantee credit) to any of such Persons, other than (i) for payment of salary for services rendered, (ii) reimbursement for reasonable expenses incurred on behalf of the Company, and (iii) for other employee benefits made generally available to all employees.

(b) Except as set forth in *Schedule 2.22*, to the Company s knowledge, none of such individuals has any direct or indirect ownership interest in any Person with whom the Company is affiliated or with whom the Company has a contractual relationship, or in any Person that competes with the Company, except that each employee, stockholder, officer or director of the Company and members of their respective immediate families may own less than 5% of the outstanding stock in publicly traded companies that may compete with the Company.

(c) Except as set forth in *Schedule 2.22*, to the knowledge of the Company, no officer, director, manager, member or stockholder or any member of their immediate families is, directly or indirectly, interested in any Material Company Contract with the Company (other than such contracts as relate to any such Person s ownership of capital stock or other securities of the Company or such Person s employment with the Company).

(d) The Company is not a guarantor to the debt or other obligations of any of its directors, officers, stockholders, members, employees or affiliates (*Company Guarantees*).

2.23 *Board Approval*. The board of directors or managers, as they case may be, of each of AAI, each CI company and LLC (including any required committee or subgroup thereof) has, as of the date of this Agreement, duly approved this Agreement and the transactions contemplated hereby.

2.24 *Stockholder or Member Approval*. The shares of Company Capital Stock owned by the Stockholder, the CI Stockholders and Lim constitute, in the aggregate, all of the outstanding capital stock of each of AAI and each CI company, and the Company Membership Interests owned by the Stockholder and Lim constitute, in the aggregate, all of the outstanding equity interest in LLC, and therefore represents, in each case, the requisite amount of shares necessary for the adoption of this Agreement and the approval of the Business Combination by the stockholders or members of each of AAI, each CI company and LLC in accordance with the Company s Charter Documents and the Applicable Corporate Laws.

2.25 *Product Liability; Product Recalls*. The Company never been found liable in a cause of action based on any product liability or related claims and has never been a party to any action alleging same. *Schedule 2.25* sets forth a detailed description of each recall of any product of the Company since January 1, 2001.

2.26 *Lim Option Agreement.* The certain agreement by and between the Stockholder and Lim, dated as of November 9, 2006 (*Lim Option Agreement*), by which the Stockholder has the right, at any time before May 1, 2006, 5:00 PM (PDT), to purchase all of the Company Capital Stock and Company Membership Interests currently owned by Lim is in full force and effect and the Stockholder is not in default thereunder.

2.27 *Privacy Matters*.

(a) Each of the CI companies carries on and has carried on its business in compliance with all applicable laws including the Personal Information Protection and Electronic Documents Act (Canada), the Personal Information Protection Act (Alberta), and the Personal Information Protection Act (British Columbia) (collectively *Privacy Laws*) relating to the protection of information about an identifiable individual which is protected by Privacy Laws (*Personal Information*) wherever such Personal Information may be situate;

(b) Where consent of an individual to the collection, use or disclosure of Personal Information is required, either by law or in accordance with the Privacy Policies such consent has been obtained in accordance with Privacy Law and with the privacy policies of each of the CI companies (the *Privacy Policies*);

(c) All Personal Information held by the CI companies was collected and is used and disclosed by the CI companies for reasonable and legitimate purposes in accordance with Applicable Law and the Privacy Policies;

(d) The CI companies have not transferred Personal Information to any agent or other third party service provider or contractor for any purpose.

(e) There are no pending or proposed changes to Privacy Laws which would render unlawful or restrict the operations of the CI companies, or any part thereof, or the manufacture, sale, distribution or provision of any products or services by the CI companies; and

(f) No Investigations, Orders or Offences. There are no current or unresolved requests for access to Personal Information and the CI companies have not been the subject of a complaint, audit, review, investigation or inquiry or similar proceeding, made under any Privacy Law.

2.28 *Representations and Warranties Complete*. The representations and warranties of the Company included in this Agreement and any list, statement, document or information set forth in, or attached to, any Schedule provided pursuant to this Agreement or delivered hereunder, are true and complete in all material respects and do not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements contained therein not misleading, under the circumstance under which they were made.

2.29 *Survival of Representations and Warranties*. The representations and warranties of the Company set forth in this Agreement shall survive the Closing until the end of the Escrow Period.

ARTICLE III

REPRESENTATIONS AND WARRANTIES OF PARENT

Subject to the exceptions set forth in *Schedule 3* attached hereto (the *Parent Schedule*), Parent represents and warrants to, and covenants with, the Company as follows:

3.1 *Organization and Qualification*.

(a) Parent is a corporation duly incorporated, validly existing and in good standing under the laws of the State of Delaware and has the requisite corporate power and authority to own, lease and operate its assets and properties and to carry on its business as it is now being or currently planned by Parent to be conducted. Parent is in possession of all Approvals necessary to own, lease and operate the properties it purports to own, operate or lease and to carry on its business as it is now being or currently planned by Parent to be conducted, except where the failure to have such Approvals could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on Parent. Complete and correct copies of the Charter Documents of Parent, as amended and currently in effect, have been heretofore delivered to the Company. Parent is not in violation of any of the provisions of Parent s Charter Documents.

(b) Parent is duly qualified or licensed to do business as a foreign corporation and is in good standing, in each jurisdiction where the character of the properties owned, leased or operated by it or the nature of its activities makes such qualification or licensing necessary, except for such failures to be so duly qualified or licensed and in good standing that could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on Parent.

3.2 *Subsidiaries*.

(a) Except for the Merger Sub, which is a wholly-owned subsidiary of Parent, Parent has no Subsidiaries and does not own, directly or indirectly, any ownership, equity, profits or voting interest in any Person or have any agreement or commitment to purchase any such interest, and Parent has not agreed and is not obligated to make nor is bound by any written, oral or other agreement, contract, subcontract, lease, binding understanding, instrument, note, option, warranty, purchase order, license, sublicense, insurance policy, benefit plan, commitment or undertaking of any nature, as of the date hereof or as may hereafter be in effect under which it may become obligated to make, any future investment in or capital contribution to any other entity.

(b) The Merger Sub is a limited liability company duly formed, validly existing and in good standing under the laws of its formation and has the requisite power and authority to own, lease and operate its assets and properties and to carry on its business as it is now being or currently planned by Parent to be conducted. The Merger Sub is not in violation of any of the provisions of its Charter Documents.

(c) The Merger Sub does not have any assets or properties of any kind, does not now conduct and has never conducted any business, and has and will have at the Closing no obligations or liabilities of any nature whatsoever except such obligations and liabilities as are imposed under this Agreement.

3.3 *Capitalization*.

(a) As of the date of this Agreement, the authorized capital stock of Parent consists of 75,000,000 shares of Parent Common Stock and 1,000,000 shares of preferred stock, par value $0.0001 per share (*Parent Preferred Stock*), of which 19,910,745 shares of Parent Common Stock and no shares of Parent Preferred Stock are issued and outstanding, all of which are validly issued, fully paid and nonassessable.

(b) Except as set forth in *Schedule* 3.*3(b)*, (i) no shares of Parent Common Stock or Parent Preferred Stock are reserved for issuance upon the exercise of outstanding options to purchase Parent Common Stock or Parent Preferred Stock granted to employees of Parent or other parties (*Parent Stock Options*) and there are no outstanding Parent Stock Options; (ii) no shares of Parent Common Stock or Parent Preferred Stock are reserved for issuance upon the exercise of outstanding warrants to purchase Parent Common Stock or Parent Preferred Stock (*Parent Warrants*) and there are no outstanding Parent Warrants; and (iii) no shares of Parent Common Stock or Parent Preferred Stock are reserved for issuance upon the conversion of the Parent Preferred Stock or any outstanding convertible notes, debentures or securities (*Parent Convertible Securities*). All shares of Parent Common Stock and Parent Preferred Stock subject to issuance as aforesaid, upon issuance on the terms and conditions specified in the instrument pursuant to which they are issuable, will be duly authorized, validly issued, fully paid and nonassessable. All outstanding shares of Parent Common Stock and all outstanding Parent Warrants have been issued and granted in compliance with (x) all applicable securities laws and (in all material respects) other applicable laws and regulations, and (y) all requirements set forth in any applicable Parent Contracts (as defined in Section 3.19). Parent has heretofore delivered to the Company true, complete and accurate copies of the Parent Warrants, including any and all documents and agreements relating thereto.

(c) The shares of Parent Common Stock to be issued by Parent in connection with the Business Combination, upon issuance in accordance with the terms of this Agreement, will be duly authorized and validly issued and such shares of Parent Common Stock will be fully paid and nonassessable.

(d) Except as set forth in *Schedule 3.3(d)* or as contemplated by this Agreement or the Parent SEC Reports (as defined in Section 3.7), there are no registrations rights, and there is no voting trust, proxy, rights plan, antitakeover plan or other agreements or understandings to which the Parent is a party or by which the Parent is bound with respect to any equity security of any class of the Parent.

(e) Except as provided for in this Agreement or as set forth in Section 3.3(e), as a result of the consummation of the transactions contemplated hereby, no shares of capital stock, warrants, options or other securities of the Parent are issuable and no rights in connection with any shares, warrants, options or other securities of the Parent accelerate or otherwise become triggered (whether as to vesting, exercisability, convertibility or otherwise).

3.4 *Authority Relative to this Agreement*. Each of Parent and the Merger Sub has full corporate power and authority to: (i) execute, deliver and perform this Agreement, and each ancillary document that Parent or the Merger Sub has executed or delivered or is to execute or deliver pursuant to this Agreement, and (ii) carry out Parent s and the Merger Sub s obligations hereunder and thereunder and, to consummate the transactions contemplated hereby (including the Business Combination). The execution and delivery of this Agreement and the consummation by Parent and the Merger Sub of the transactions contemplated hereby (including the Business Combination) have been duly and validly authorized by all necessary corporate action on the part of Parent and

Table of Contents

the Merger Sub (including the approval by their respective Boards of Directors), and no other corporate proceedings on the part of Parent or any of the Merger Sub are necessary to authorize this Agreement or to consummate the transactions contemplated hereby, other than the Parent Stockholder Approval (as defined in Section 5.1(b)). This Agreement has been duly and validly executed and delivered by Parent and the Merger Sub and, assuming the due authorization, execution and delivery thereof by the other parties hereto, constitutes the legal and binding obligation of Parent and the Merger Sub, enforceable against Parent and the Merger Sub in accordance with its terms, except as may be limited by bankruptcy, insolvency, reorganization or other similar laws affecting the enforcement of creditors rights generally and by general principles of equity.

3.5 *No Conflict; Required Filings and Consents*.

(a) The execution and delivery of this Agreement by Parent and the Merger Sub do not, and the performance of this Agreement by Parent and the Merger Sub shall not: (i) conflict with or violate Parent s or the Merger Sub s Charter Documents, (ii) conflict with or violate any Legal Requirements, or (iii) result in any breach of or constitute a default (or an event that with notice or lapse of time or both would become a default) under, or materially impair Parent s or the Merger Sub s rights or alter the rights or obligations of any third party under, or give to others any rights of termination, amendment, acceleration or cancellation of, or result in the creation of a Lien on any of the properties or assets of Parent pursuant to, any Parent Contracts, except, with respect to clauses (ii) or (iii), for any such conflicts, violations, breaches, defaults or other occurrences that would not, individually and in the aggregate, have a Material Adverse Effect on Parent.

(b) The execution and delivery of this Agreement by Parent and the Merger Sub do not, and the performance of their respective obligations hereunder will not, require any consent, approval, authorization or permit of, or filing with or notification to, any Governmental Entity, except (i) for applicable requirements, if any, of the Securities Act, the Exchange Act, Blue Sky Laws, and the rules and regulations thereunder, and appropriate documents with the relevant authorities of other jurisdictions in which Parent or Merger Sub is qualified to do business, (ii) for the filing of any notifications required under the HSR Act and the expiration of the required waiting period thereunder, (iii) the filing of the Section 116 Certificate and (iv) where the failure to obtain such consents, approvals, authorizations or permits, or to make such filings or notifications, would not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect on Parent, or prevent consummation of the Business Combination or otherwise prevent the parties hereto from performing their obligations under this Agreement.

3.6 *Compliance*. Parent has complied with, and is not in violation of, any Legal Requirements with respect to the conduct of its business, or the ownership or operation of its business, except for failures to comply or violations which, individually or in the aggregate, have not had and are not reasonably likely to have a Material Adverse Effect on Parent. The business and activities of Parent have not been and are not being conducted in violation of any Legal Requirements. Parent is not in default or violation of any term, condition or provision of its Charter Documents. No written notice of non-compliance with any Legal Requirements has been received by Parent.

3.7 *SEC Filings; Financial Statements*.

(a) Parent has made available to the Company and the Stockholder the CI Stockholders and Lim a correct and complete copy of each report and registration statement filed by Parent with the SEC (the *Parent SEC Reports*), which are all the forms, reports and documents required to be filed by Parent with the SEC prior to the date of this Agreement. All Parent SEC Reports required to be filed by Parent in the twelve (12) month period prior to the date of this Agreement were filed in a timely manner. As of their respective dates the Parent SEC Reports: (i) were prepared in accordance and complied in all material respects with the requirements of the Securities Act or the Exchange Act, as the case may be, and the rules and regulations of the SEC thereunder applicable to such Parent SEC Reports, and (ii) did not at the time they were filed (and if amended or superseded by a filing prior to the date of this Agreement then on the date of such filing and as so amended or superseded) contain any untrue statement of a material fact or omit

Table of Contents

to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they were made, not misleading. Except to the extent set forth in the preceding sentence, Parent makes no representation or warranty whatsoever concerning any Parent SEC Report as of any time other than the date or period with respect to which it was filed.

(b) Except as set forth in *Schedule 3.7(b)*, each set of financial statements (including, in each case, any related notes thereto) contained in Parent SEC Reports, including each Parent SEC Report filed after the date hereof until the Closing, complied or will comply as to form in all material respects with the published rules and regulations of the SEC with respect thereto, was or will be prepared in accordance with U.S. GAAP applied on a consistent basis throughout the periods involved (except as may be indicated in the notes thereto or, in the case of unaudited statements, do not contain footnotes as permitted by Form 10-QSB of the Exchange Act) and each fairly presents or will fairly present in all material respects the financial position of Parent at the respective dates thereof and the results of its operations and cash flows for the periods indicated, except that the unaudited interim financial statements were, are or will be subject to normal adjustments which were not or are not expected to have a Material Adverse Effect on Parent taken as a whole.

3.8 *No Undisclosed Liabilities*. Parent has no liabilities (absolute, accrued, contingent or otherwise) of a nature required to be disclosed on a balance sheet or in the related notes to the financial statements included in Parent SEC Reports that are, individually or in the aggregate, material to the business, results of operations or financial condition of Parent, except (i) liabilities provided for in or otherwise disclosed in Parent SEC Reports filed prior to the date hereof, and (ii) liabilities incurred since January 1, 2006 in the ordinary course of business, none of which would have a Material Adverse Effect on Parent.

3.9 *Absence of Certain Changes or Events*. Except as set forth in Parent SEC Reports filed prior to the date of this Agreement, and except as contemplated by this Agreement, since January 1, 2006, there has not been: (i) any Material Adverse Effect on Parent, (ii) any declaration, setting aside or payment of any dividend on, or other distribution (whether in cash, stock or property) in respect of, any of Parent s capital stock, or any purchase, redemption or other acquisition by Parent of any of Parent s capital stock or any other securities of Parent or any options, warrants, calls or rights to acquire any such shares or other securities, (iii) any split, combination or reclassification of any of Parent s capital stock, (iv) any granting by Parent of any increase in compensation or fringe benefits, except for normal increases of cash compensation in the ordinary course of business consistent with past practice, or any payment by Parent of any bonus, except for bonuses made in the ordinary course of business consistent with past practice, or any granting by Parent of any increase in severance or termination pay or any entry by Parent into any currently effective employment, severance, termination or indemnification agreement or any agreement the benefits of which are contingent or the terms of which are materially altered upon the occurrence of a transaction involving Parent of the nature contemplated hereby, (v) entry by Parent into any licensing or other agreement with regard to the acquisition or disposition of any Intellectual Property other than licenses in the ordinary course of business consistent with past practice or any amendment or consent with respect to any licensing agreement filed or required to be filed by Parent with respect to any Governmental Entity, (vi) any material change by Parent in its accounting methods, principles or practices, except as required by concurrent changes in U.S. GAAP, (vii) any change in the auditors of Parent, (vii) any issuance of capital stock of Parent, or (viii) any revaluation by Parent of any of its assets, including, without limitation, writing down the value of capitalized inventory or writing off notes or accounts receivable or any sale of assets of Parent other than in the ordinary course of business.

3.10 *Litigation*. There are no claims, suits, actions or proceedings pending or to Parent s knowledge, threatened against Parent, before any court, governmental department, commission, agency, instrumentality or authority, or any arbitrator that seeks to restrain or enjoin the consummation of the transactions contemplated by this Agreement or which could reasonably be expected, either singularly or in the aggregate with all such claims, actions or proceedings, to have a Material Adverse Effect on Parent or have a Material Adverse Effect on the ability of the parties hereto to consummate the Business Combination.

Table of Contents

3.11 *Employee Benefit Plans*. Except as may be contemplated by the Parent Plan (as defined in Section 5.1(b)), Parent does not maintain, and has no liability under, any Plan, and neither the execution and delivery of this Agreement nor the consummation of the transactions contemplated hereby will (i) result in any payment (including severance, unemployment compensation, golden parachute, bonus or otherwise) becoming due to any stockholder, director or employee of Parent, or (ii) result in the acceleration of the time of payment or vesting of any such benefits.

3.12 *Labor Matters*. Parent is not a party to any collective bargaining agreement or other labor union contract applicable to persons employed by Parent and Parent does not know of any activities or proceedings of any labor union to organize any such employees.

3.13 *Restrictions on Business Activities*. Since its organization, Parent has not conducted any business activities other than activities directed toward the accomplishment of a business combination. Except as set forth in the Parent Charter Documents, there is no agreement, commitment, judgment, injunction, order or decree binding upon Parent or to which Parent is a party which has or could reasonably be expected to have the effect of prohibiting or materially impairing any business practice of Parent, any acquisition of property by Parent or the conduct of business by Parent as currently conducted other than such effects, individually or in the aggregate, which have not had and could not reasonably be expected to have, a Material Adverse Effect on Parent.

3.14 *Title to Property*. Parent does not own or lease any real property or personal property. Except as set forth in *Schedule 3.14*, there are no options or other contracts under which Parent has a right or obligation to acquire or lease any interest in real property or personal property.

3.15 *Taxes*. Except as set forth in *Schedule 3.15* hereto:

(a) Parent has timely filed all Returns required to be filed by Parent with any Tax authority prior to the date hereof, except such Returns which are not material to Parent. All such Returns are true, correct and complete in all material respects. Parent has paid all Taxes shown to be due on such Returns.

(b) All Taxes that Parent is required by law to withhold or collect have been duly withheld or collected, and have been timely paid over to the proper governmental authorities to the extent due and payable.

(c) Parent has not been delinquent in the payment of any material Tax that has not been accrued for in Parent s books and records of account for the period for which such Tax relates nor is there any material Tax deficiency outstanding, proposed or assessed against Parent, nor has Parent executed any unexpired waiver of any statute of limitations on or extending the period for the assessment or collection of any Tax.

(d) No audit or other examination of any Return of Parent by any Tax authority is presently in progress, nor has Parent been notified of any request for such an audit or other examination.

(e) No adjustment relating to any Returns filed by Parent has been proposed in writing, formally or informally, by any Tax authority to Parent or any representative thereof.

(f) Parent has no liability for any material unpaid Taxes which have not been accrued for or reserved on Parent s balance sheets included in the audited financial statements for the most recent fiscal year ended, whether asserted or unasserted, contingent or otherwise, which is material to Parent, other than any liability for unpaid Taxes that may have accrued since the end of the most recent fiscal year in connection with the operation of the business of Parent in the ordinary course of business, none of which is material to the business, results of operations or financial condition of Parent.

(g) Parent has not taken any action and does not know of any fact, agreement, plan or other circumstance that is reasonably likely to prevent the Merger and each Canada Acquisition from qualifying as a reorganization within the meaning of Section 368(a) of the Code.

Table of Contents

3.16 *Environmental Matters*. Except for such matters that, individually or in the aggregate, are not reasonably likely to have a Material Adverse Effect: (i) Parent has complied with all applicable Environmental Laws; (ii) Parent is not subject to liability for any Hazardous Substance disposal or contamination on any third party property; (iii) Parent has not been associated with any release or threat of release of any Hazardous Substance; (iv) Parent has not received any notice, demand, letter, claim or request for information alleging that Parent may be in violation of or liable under any Environmental Law; and (v) Parent is not subject to any orders, decrees, injunctions or other arrangements with any Governmental Entity or subject to any indemnity or other agreement with any third party relating to liability under any Environmental Law or relating to Hazardous Substances.

3.17 *Brokers*. Except as set forth in *Schedule 3.17*, Parent has not incurred, nor will it incur, directly or indirectly, any liability for brokerage or finders fees or agent s commissions or any similar charges in connection with this Agreement or any transaction contemplated hereby.

3.18 *Intellectual Property*. Parent does not own, license or otherwise have any right, title or interest in any material Intellectual Property or material Registered Intellectual Property, except non-exclusive rights to the name Endeavor and SPAC .

3.19 *Agreements, Contracts and Commitments*.

(a) Except as set forth in the Parent SEC Reports filed prior to the date of this Agreement, and with respect to confidentiality and nondisclosure agreements, there are no contracts, agreements, leases, mortgages, indentures, notes, bonds, liens, license, permit, franchise, purchase orders, sales orders or other understandings, commitments or obligations (including without limitation outstanding offers or proposals) of any kind, whether written or oral, to which Parent is a party or by or to which any of the properties or assets of Parent may be bound, subject or affected, which either (a) creates or imposes a liability greater than $25,000, or (b) may not be cancelled by Parent on 30 days or less prior notice (*Parent Contracts*). All Parent Contracts are listed in *Schedule 3.19* other than those that are exhibits to the Parent SEC Reports.

(b) Except as set forth in the Parent SEC Reports filed prior to the date of this Agreement, each Parent Contract was entered into at arms length and in the ordinary course, is in full force and effect and is valid and binding upon and enforceable against each of the parties thereto. True, correct and complete copies of all Parent Contracts (or written summaries in the case of oral Parent Contracts) and of all outstanding offers or proposals of Parent have been heretofore delivered to the Company.

(c) Neither Parent nor, to the knowledge of Parent, any other party thereto is in breach of or in default under, and no event has occurred which with notice or lapse of time or both would become a breach of or default under, any Parent Contract, and no party to any Parent Contract has given any written notice of any claim of any such breach, default or event, which, individually or in the aggregate, are reasonably likely to have a Material Adverse Effect on Parent. Each agreement, contract or commitment to which Parent is a party or by which it is bound that has not expired by its terms is in full force and effect, except where such failure to be in full force and effect is not reasonably likely to have a Material Adverse Effect on Parent.

3.20 *Insurance*. Except for directors and officers liability insurance, Parent does not maintain any Insurance Policies.

3.21 *Interested party Transactions*. Except as set forth in the Parent SEC Reports filed prior to the date of this Agreement: (a) no employee, officer, director or stockholder of Parent or a member of his or her immediate family is indebted to Parent nor is Parent indebted (or committed to make loans or extend or guarantee credit) to any of them, other than reimbursement for reasonable expenses incurred on behalf of Parent; (b) to Parent s knowledge, none of such individuals has any direct or indirect ownership interest in any Person with whom Parent is affiliated or with whom Parent has a material contractual relationship, or any Person that competes with Parent, except that each employee, stockholder, officer or director of Parent and members of their respective

A-28

immediate families may own less than 5% of the outstanding stock in publicly traded companies that may compete with Parent; and (c) to Parent s knowledge, no officer, director or stockholder or any member of their immediate families is, directly or indirectly, interested in any material contract with Parent (other than such contracts as relate to any such individual ownership of capital stock or other securities of Parent).

3.22 *Indebtedness. Parent has no indebtedness for borrowed money.*

3.23 *American Stock Exchange Quotation*. Parent Common Stock is quoted on the American Stock Exchange (*AMEX*). There is no action or proceeding pending or, to Parent s knowledge, threatened against Parent by the American Stock Exchange with respect to any intention by such entity to prohibit or terminate the quotation of such securities thereon.

3.24 *Board Approval*. The Board of Directors of Parent (including any required committee or subgroup of the Board of Directors of Parent) has, as of the date of this Agreement, unanimously (i) declared the advisability of the Business Combination and approved this Agreement and the transactions contemplated hereby, (ii) determined that the Business Combination is in the best interests of the stockholders of Parent, and (iii) determined that the fair market value of the Company is equal to at least 80% of Parent s net assets.

3.25 *Trust Fund*. As of the date hereof and at the Closing Date, Parent has and will have no less than $124,043,336 invested in United States government securities within the meaning of Section 2(a)(16) of the Investment Company Act of 1940 having a maturity of 180 days or less, or in money market funds meeting certain conditions under Rule 2a-7 promulgated under the Investment Company Act of 1940 in a trust account administered by Escrow Agent (the *Trust Fund*), less any amounts contemplated as being deducted from or reserved against such Trust Fund in Section 5.25 of this Agreement.

3.26 *Governmental Filings*. Except as set forth in *Schedule 3.26*, Parent has been granted and holds, and has made, all Governmental Actions/Filings necessary to the conduct by Parent of its business (as presently conducted) or used or held for use by Parent, and true, complete and correct copies of which have heretofore been delivered to the Company. Each such Governmental Action/Filing is in full force and effect and, except as disclosed in *Schedule 3.26*, will not expire prior to December 31, 2008, and Parent is in compliance with all of its obligations with respect thereto. No event has occurred and is continuing which requires or permits, or after notice or lapse of time or both would require or permit, and consummation of the transactions contemplated by this Agreement or any ancillary documents will not require or permit (with or without notice or lapse of time, or both), any modification or termination of any such Governmental Actions/Filings except such events which, either individually or in the aggregate, would not have a Material Adverse Effect upon Parent.

3.27 *WTO Investor*. Parent is a WTO Investor under the Investment Canada Act.

3.28 *Representations and Warranties Complete*. The representations and warranties of Parent included in this Agreement and any list, statement, document or information set forth in, or attached to, any Schedule provided pursuant to this Agreement or delivered hereunder, are true and complete in all material respects and do not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements contained therein not misleading, under the circumstance under which they were made.

3.29 *Survival of Representations and Warranties*. The representations and warranties of Parent set forth in this Agreement shall survive until the Closing.

ARTICLE IV

CONDUCT PRIOR TO THE EFFECTIVE TIME

4.1 *Conduct of Business by the Company and Parent*. During the period from the date of this Agreement and continuing until the earlier of the termination of this Agreement pursuant to its terms or the Closing, each of the Company, the Stockholder, Parent and the Merger Sub shall, except to the extent that the other party shall otherwise consent in writing, carry on its business in the usual, regular and ordinary course consistent with past practices, in substantially the same manner as heretofore conducted and in compliance with all applicable laws and regulations (except where noncompliance would not have a Material Adverse Effect), pay its debts and taxes when due subject to good faith disputes over such debts or taxes, pay or perform other material obligations when due, and use its best efforts consistent with past practices and policies to (i) preserve substantially intact its present business organization, (ii) keep available the services of its present officers and employees and (iii) preserve its relationships with customers, suppliers, distributors, licensors, licensees, and others with which it has significant business dealings. In addition, except as required or permitted by the terms of this Agreement, without the prior written consent of the other party, during the period from the date of this Agreement and continuing until the earlier of the termination of this Agreement pursuant to its terms or the Closing, each of the Company, the Stockholder, Parent and the Merger Sub shall not do any of the following:

(a) Waive any stock repurchase rights, accelerate, amend or (except as specifically provided for herein) change the period of exercisability of options or restricted stock, or reprice options granted under any employee, consultant, director or other stock plans or authorize cash payments in exchange for any options granted under any of such plans;

(b) Grant any severance or termination pay to any officer or employee except pursuant to applicable law, written agreements outstanding, or policies existing on the date hereof and as previously or concurrently disclosed in writing or made available to the other party, or adopt any new severance plan, or amend or modify or alter in any manner any severance plan, agreement or arrangement existing on the date hereof;

(c) Transfer or license to any person or otherwise extend, amend or modify any material rights to any Intellectual Property of the Company or Parent, as applicable, or enter into grants to transfer or license to any person future patent rights, other than in the ordinary course of business consistent with past practices provided that in no event shall the Company or Parent license on an exclusive basis or sell any Intellectual Property of the Company, or Parent as applicable;

(d) Declare, set aside or pay any dividends on or make any other distributions (whether in cash, stock, equity securities or property) in respect of any capital stock or split, combine or reclassify any capital stock or issue or authorize the issuance of any other securities in respect of, in lieu of or in substitution for any capital stock; provided, however, that AAI shall be permitted to make distributions of Stub Period Tax Amounts to the Stockholder and Lim in accordance with Section 1.15;

(e) Purchase, redeem or otherwise acquire, directly or indirectly, any shares of capital stock of the Company and Parent, as applicable, including repurchases of unvested shares at cost in connection with the termination of the relationship with any employee or consultant pursuant to agreements in effect on the date hereof;

(f) Issue, deliver, sell, authorize, pledge or otherwise encumber, or agree to any of the foregoing with respect to, any shares of capital stock or any securities convertible into or exchangeable for shares of capital stock, or subscriptions, rights, warrants or options to acquire any shares of capital stock or any securities convertible into or exchangeable for shares of capital stock, or enter into other agreements or commitments of any character obligating it to issue any such shares or convertible or exchangeable securities;

(g) Amend its Charter Documents;

Table of Contents

(h) Acquire or agree to acquire by merging or consolidating with, or by purchasing any equity interest in or a portion of the assets of, or by any other manner, any business or any corporation, partnership, association or other business organization or division thereof, or otherwise acquire or agree to acquire any assets which are material, individually or in the aggregate, to the business of Parent or the Company as applicable, or enter into any joint ventures, strategic partnerships or alliances or other arrangements that provide for exclusivity of territory or otherwise restrict such party s ability to compete or to offer or sell any products or services;

(i) Sell, lease, license, encumber or otherwise dispose of any properties or assets, except (A) sales of inventory in the ordinary course of business consistent with past practice, and (B) the sale, lease or disposition (other than through licensing) of property or assets that are not material, individually or in the aggregate, to the business of such party;

(j) Except as disclosed in *Schedule 2.22* and except for borrowing under the Company s existing credit facilities in the ordinary course of business or any new borrowing arrangements entered into by the Company for the purpose of operating the business in the ordinary course or replacing currently existing mezzanine borrowing in the approximate amount of $15 million with C3 Capital Partners and syndicated lenders, incur any indebtedness for borrowed money in excess of $25,000 in the aggregate or guarantee any such indebtedness of another person, issue or sell any debt securities or options, warrants, calls or other rights to acquire any debt securities of Parent or the Company, as applicable, enter into any keep well or other agreement to maintain any financial statement condition or enter into any arrangement having the economic effect of any of the foregoing, nor shall the Company modify or terminate any of its existing credit facilities;

(k) Adopt or amend any employee benefit plan, policy or arrangement, any employee stock purchase or employee stock option plan, or enter into any employment contract or collective bargaining agreement (other than offer letters and letter agreements entered into in the ordinary course of business consistent with past practice with employees who are terminable at will), pay any special bonus or special remuneration to any director or employee, or increase the salaries or wage rates or fringe benefits (including rights to severance or indemnification) of its directors, officers, employees or consultants, except in the ordinary course of business consistent with past practices;

(l) Pay, discharge, settle or satisfy any claims, liabilities or obligations (absolute, accrued, asserted or unasserted, contingent or otherwise), or litigation (whether or not commenced prior to the date of this Agreement) other than the payment, discharge, settlement or satisfaction, in the ordinary course of business consistent with past practices or in accordance with their terms, or liabilities recognized or disclosed in the Stub Financial Statements or in the most recent financial statements included in the Parent SEC Reports filed prior to the date of this Agreement, as applicable, or incurred since the date of such financial statements, or waive the benefits of, agree to modify in any manner, terminate, release any person from or knowingly fail to enforce any confidentiality or similar agreement to which the Company is a party or of which the Company is a beneficiary or to which Parent is a party or of which Parent is a beneficiary, as applicable;

(m) Except in the ordinary course of business consistent with past practices, modify, amend or terminate any Company Contract or Parent Contract, as applicable, or waive, delay the exercise of, release or assign any material rights or claims thereunder;

(n) Except as required by U.S. GAAP, revalue any of its assets or make any change in accounting methods, principles or practices;

(o) Except in the ordinary course of business consistent with past practices, incur or enter into any agreement, contract or commitment requiring such party to pay in excess of $100,000 in any 12 month period;

(p) Engage in any action that could reasonably be expected to cause the Merger or any Canada Acquisition to fail to qualify as a reorganization under Section 368(a) of the Code;

(q) Settle any litigation to which an Insider is a party or where the consideration given by the Company is other than monetary;

(r) Make or rescind any Tax elections that, individually or in the aggregate, could be reasonably likely to adversely affect in any material respect the Tax liability or Tax attributes of such party, settle or compromise any material income tax liability or, except as required by applicable law, materially change any method of accounting for Tax purposes or prepare or file any Return in a manner inconsistent with past practice;

(s) Form, establish or acquire any subsidiary except as contemplated by this Agreement;

(t) Permit any Person to exercise any of its discretionary rights under any Plan to provide for the automatic acceleration of any outstanding options, the termination of any outstanding repurchase rights or the termination of any cancellation rights issued pursuant to such plans;

(u) Make capital expenditures except in accordance with prudent business and operational practices consistent with prior practice;

(v) Make or omit to take any action which would be reasonably anticipated to have a Material Adverse Effect;

(w) Except as disclosed in *Schedule 2.22*, enter into any transaction with or distribute or advance any assets or property to any of its officers, directors, partners, stockholders or other affiliates other than the payment of salary and benefits in the ordinary course of business consistent with past practice; or

(x) Agree in writing or otherwise agree, commit or resolve to take any of the actions described in Section 4.1 (a) through (w) above.

4.2 *Exclusivity*.

(a) Each of the Stockholder, each CI Stockholder and Lim, and the Company shall not, and the Company shall use reasonable best efforts to cause each of its officers, directors, employees, representatives and agents not to, directly or indirectly, (i) encourage, solicit, initiate, engage or participate in negotiations with any person or entity (other than the Parent) concerning any Acquisition Transaction or (ii) take any other action intended or designed to facilitate the efforts of any person or entity (other than Parent) relating to a possible Acquisition Transaction. For purposes of this Agreement, the term *Acquisition Transaction* shall mean any of the following involving the Company or any subsidiary of the Company: (i) any merger, consolidation, share exchange, business combination or other similar transaction; or (ii) any sale, lease, exchange, transfer or other disposition of any of the assets of the Company or Subsidiaries (other than in the normal course of business consistent with past practice) or any shares of the capital stock of the Company or any Subsidiary in a single transaction or series of transactions.

(b) In the event that there is an unsolicited proposal for or an unsolicited indication of a serious interest in entering into, an Acquisition Transaction, communicated to the Company, the Stockholder, any CI Stockholder or Lim or any of their representatives or agents, such party shall immediately (and in no less than 48 hours) give written notice of same to the Parent.

Table of Contents

ARTICLE V

ADDITIONAL AGREEMENTS

5.1 *Audited Financials; Proxy Statement; Special Meeting*.

(a) Intentionally Omitted.

(b) As soon as is reasonably practicable after receipt by Parent from the Company of all financial information required for the proxy materials discussed below and other information relating to the Company as Parent may reasonably request for its preparation, and the Fairness Opinion (as defined) has been obtained by Parent from a qualified investment bank, Parent shall prepare and file with the SEC under the Exchange Act, and with all other applicable regulatory bodies, proxy materials for the purpose of soliciting proxies from holders of Parent Common Stock to vote in favor of: (i) the adoption of this Agreement and the approval of the Business Combination (*Parent Stockholder Approval*); (ii) the change of the name of Parent to a name selected by the Company (the *Name Change Amendment*); (iii) an increase in the number of authorized shares of Parent Common Stock to 120 million shares (the *Capitalization Amendment*); (iv) an amendment to remove the preamble and Sections A through D, inclusive, of Article Sixth from Parent s Certificate of Incorporation from and after the Closing and to redesignate and restate Section E as Article Sixth and to otherwise ensure that the provisions contemplated by the Voting Agreement are permitted; and (v) the adoption of a Performance Equity Plan in form and substance reasonably acceptable to Parent and the Stockholder (*Parent Plan*), at a meeting of holders of Parent Common Stock to be called and held for such purpose (the *Special Meeting*). The Parent Plan shall provide that an aggregate of 7,710,000 shares of Parent Common Stock shall be reserved for issuance pursuant to the Parent Plan. Such proxy materials shall be in the form of a proxy statement to be used for the purpose of soliciting such proxies from holders of Parent Common Stock (the *Proxy Statement*). The Company shall furnish to Parent on a timely basis all information concerning the Company (or any of the Subsidiaries) as Parent may reasonably request in connection with the preparation of the Proxy Statement. The Company and its counsel shall be given an opportunity to review, comment on and approve (which such approval shall not be unreasonably withheld, delayed or conditioned) the Proxy Statement prior to its filing with the SEC. Parent, with the assistance of the Company, shall promptly respond to any SEC comments on the Proxy Statement and shall otherwise use best efforts to cause the Proxy Statement to be approved for issuance by the SEC as promptly as practicable. Parent shall also take any and all such actions to satisfy the requirements of the Securities Act and the Exchange Act. Prior to the Closing Date, Parent shall use its best efforts to cause the shares of Parent Common Stock to be issued pursuant to the Business Combination to be registered or qualified under all applicable Blue Sky Laws of each of the states and territories of the United States in which it is believed, based on information furnished by the company, holders of the Company Capital Stock reside and to take any other such actions that may be necessary to enable the Parent Common Stock to be issued pursuant to the Business Combination in each such jurisdiction.

(c) As soon as practicable following its approval by the Commission, Parent shall distribute the Proxy Statement to the holders of Parent Common Stock and, pursuant thereto, shall call the Special Meeting in accordance with the Delaware General Corporate Law (*DGCL*) and, subject to the other provisions of this Agreement, solicit proxies from such holders to vote in favor of the adoption of this Agreement and the approval of the Business Combination and the other matters presented to the stockholders of Parent for approval or adoption at the Special Meeting.

(d) Parent shall comply with all applicable provisions of and rules under the Exchange Act and all applicable provisions of the DGCL in the preparation, filing and distribution of the Proxy Statement, the solicitation of proxies thereunder, and the calling and holding of the Special Meeting. Without limiting the foregoing, Parent shall ensure that the Proxy Statement does not, as of the date on which it is distributed to the holders of Parent Common Stock, and as of the date of the Special Meeting, contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading (provided that Parent shall not be

Table of Contents

responsible for the accuracy or completeness of any information relating to the Company or any other information furnished by the Company for inclusion in the Proxy Statement). The Company represents and warrants that the information relating to the Company (and the Subsidiaries) supplied by the Company for inclusion in the Proxy Statement will not as of date of its distribution to the holders of Parent Common Stock (or any amendment or supplement thereto) or at the time of the Special Meeting contain any statement which, at such time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact, or omits to state any material fact required to be stated therein or necessary in order to make the statement therein not false or misleading.

(e) Parent, acting through its board of directors, shall include in the Proxy Statement the recommendation of its board of directors that the holders of Parent Common Stock vote in favor of the adoption of this Agreement and the approval of the Business Combination, and shall otherwise use best efforts to obtain the Parent Stockholder Approval.

(f) The Company also shall cooperate with Parent and provide all information reasonably requested by Parent in connection with any application or other filing made to maintain or secure listing of Parent s securities on the American Stock Exchange, Nasdaq, OTC-BB or other exchange or trading market.

5.2 *Directors and Officers of Parent and the Surviving Corporations.* Subject to limitations imposed under applicable laws, the parties shall take all necessary actions so that the persons listed in *Schedule 5.2* (as same shall be completed prior to Closing) are elected to the positions of officers and directors of Parent and U.S. Surviving Corporation, effective immediately after the Closing. The Stockholder and those stockholders of Parent stated to be parties thereto shall enter into a Voting Agreement in the form of *Exhibit C* hereto concurrently with the execution of this Agreement.

5.3 *Public Disclosure.* From the date of this Agreement until Closing or termination, the parties shall cooperate in good faith to jointly prepare all press releases and public announcements pertaining to this Agreement and the transactions governed by it, and no party shall issue or otherwise make any public announcement or communication pertaining to this Agreement or the transaction without the prior consent of Parent (in the case of the Company and the Stockholder) or the Company (in the case of Parent and Merger Sub), except as required by any legal requirement or by the rules and regulations of, or pursuant to any agreement of a stock exchange or trading system. Each party will not unreasonably delay, withhold or condition approval from the others with respect to any press release or public announcement. If any party determines with the advice of counsel that it is required to make this Agreement and the terms of the transaction public or otherwise issue a press release or make public disclosure with respect thereto, it shall, at a reasonable time before making any public disclosure, consult with the other party regarding such disclosure, seek such confidential treatment for such terms or portions of this Agreement or the transaction as may be reasonably requested by the other party and disclose only such information as is legally compelled to be disclosed. This provision will not apply to communications by any party to its counsel, accountants and other professional advisors.

5.4 *Other Actions.*

(a) As promptly as practicable after execution of this Agreement, Parent will prepare and file a Current Report on Form 8-K pursuant to the Exchange Act to report the execution of this Agreement (*Signing Form 8-K*), which the Company may review and comment upon prior to filing. Any language included in such Current Report that reflects the Company s comments, as well as any text as to which the Company has not commented upon being given a reasonable opportunity to comment, shall, notwithstanding the provisions of Section 5.3, be deemed to have been approved by the Company and may henceforth be used by Parent in other filings made by it with the SEC and in other documents distributed by Parent in connection with the transactions contemplated by this Agreement without further review or consent of the Stockholder or the Company. Promptly after the execution of this Agreement, Parent and the Company shall also issue a press release announcing the execution of this Agreement (*Press Release*).

(b) At least five (5) days prior to Closing, Parent shall prepare a draft Form 8-K announcing the Closing, together with, or incorporating by reference, the financial statements prepared by the Company and such other information that may be required to be disclosed with respect to the Business Combination in any report or form to be filed with the SEC (*Closing Form 8-K*), which shall be in a form reasonably acceptable to the Company and in a format acceptable for EDGAR filing. Prior to Closing, Parent and the Company shall prepare the press release announcing the consummation of the Business Combination hereunder (*Closing Press Release*). Concurrently with the Closing, Parent shall file the Closing Form 8-K with the SEC and distribute the Closing Press Release.

5.5 *Required Information*. In connection with the preparation of the Signing Form 8-K, Closing Form 8-K and Press Release, or any other statement, filing, notice or application made by or on behalf of Parent and/or the Company to any third party and/or any Governmental Entity in connection with the Business Combination or the other transactions contemplated hereby, and for such other reasonable purposes, the Company and Parent each shall, upon request by the other, furnish the other with all information concerning themselves, their respective directors, officers and stockholders (including the directors of Parent and the Company to be elected effective as of the Closing pursuant to Section 5.2 hereof) and such other matters as may be reasonably necessary or advisable in connection with the Business Combination. Each party warrants and represents to the other party that all such information shall be true and correct in all material respects and will not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements contained therein, in light of the circumstances under which they were made, not misleading.

5.6 *Confidentiality; Access to Information*.

(a) *Confidentiality.* Any confidentiality agreement previously executed by the parties shall be superseded in its entirety by the provisions of this Agreement. Each party agrees to maintain in confidence any non-public information received from the other party, and to use such non-public information only for purposes of consummating the transactions contemplated by this Agreement. Such confidentiality obligations will not apply to (i) information which was known to the one party or their respective agents prior to receipt from the other party; (ii) information which is or becomes generally known; (iii) information acquired by a party or their respective agents from a third party who was not bound to an obligation of confidentiality; and (iv) disclosure required by law. In the event this Agreement is terminated as provided in Article VIII hereof, each party (i) will destroy or return or cause to be returned to the other all documents and other material obtained from the other in connection with the Business Combination contemplated hereby, and (ii) will use its reasonable best efforts to delete from its computer systems all documents and other material obtained from the other in connection with the Business Combination contemplated hereby.

(b) *Access to Information.*

(i) The Company will afford Parent and its financial advisors, accountants, counsel and other representatives reasonable access during normal business hours, upon reasonable notice, to the properties, books, records and personnel of the Company during the period prior to the Closing to obtain all information concerning the business, including the status of product development efforts, properties, results of operations and personnel of the Company, as Parent may reasonably request. No information or knowledge obtained by Parent in any investigation pursuant to this Section 5.6 will affect or be deemed to modify any representation or warranty contained herein or the conditions to the obligations of the parties to consummate the Business Combination.

(ii) Parent will afford the Company and its financial advisors, underwriters, accountants, counsel and other representatives reasonable access during normal business hours, upon reasonable notice, to the properties, books, records and personnel of Parent during the period prior to the Closing to obtain all information concerning the business, including the status of business or product development efforts, properties, results of operations and personnel of Parent, as the Company may reasonably request. No information or knowledge obtained by the Company in any investigation pursuant to this Section 5.6 will affect or be deemed to modify any representation or warranty contained herein or the conditions to the obligations of the parties to consummate the Business Combination.

5.7 *Cashless Exercise of Warrants*. The parties hereto agree that, in connection with any redemption of Parent s outstanding warrants, Parent shall offer holders thereof the opportunity to exercise such warrants on a cashless basis.

5.8 *Best Efforts*.

(a) Upon the terms and subject to the conditions set forth in this Agreement, each of Parent, the Merger Sub, the Company and the Stockholder agrees to use its best efforts to take, or cause to be taken, all actions, and to do, or cause to be done, and to assist and cooperate with the other parties in doing, all things necessary, proper or advisable to consummate and make effective, in the most expeditious manner practicable, the Business Combination and the other transactions contemplated by this Agreement, including using best efforts to accomplish the following: (i) the taking of all reasonable acts necessary to cause the conditions precedent set forth in Article VI to be satisfied, (ii) the obtaining of all necessary actions, waivers, consents, approvals, orders and authorizations from Governmental Entities and the making of all necessary registrations, declarations and filings (including registrations, declarations and filings with Governmental Entities, if any) and the taking of all reasonable steps as may be necessary to avoid any suit, claim, action, investigation or proceeding by any Governmental Entity, (iii) the obtaining of all consents, approvals or waivers from third parties required as a result of the transactions contemplated in this Agreement, including without limitation the consents referred to in *Schedule 2.5* of the Company Disclosure Schedule, (iv) the defending of any suits, claims, actions, investigations or proceedings, whether judicial or administrative, challenging this Agreement or the consummation of the transactions contemplated hereby, including seeking to have any stay or temporary restraining order entered by any court or other Governmental Entity vacated or reversed and (v) the execution or delivery of any additional instruments reasonably necessary to consummate the transactions contemplated by, and to fully carry out the purposes of, this Agreement. In connection with and without limiting the foregoing, Parent and its board of directors and each of AAI and each CI company and its respective board of directors shall, if any state or provincial takeover statute or similar statute or regulation is or becomes applicable to the Business Combination, this Agreement or any of the transactions contemplated by this Agreement, use its best efforts to enable the Business Combination and the other transactions contemplated by this Agreement to be consummated as promptly as practicable on the terms contemplated by this Agreement. Notwithstanding anything herein to the contrary, nothing in this Agreement shall be deemed to require Parent or the Company to agree to any divestiture by itself or any of its affiliates of shares of capital stock or of any business, assets or property, or the imposition of any material limitation on the ability of any of them to conduct their business or to own or exercise control of such assets, properties and stock.

(b) Each of the Company, the Stockholder and Parent shall further cooperate with each other and use their respective best efforts to take or cause to be taken all actions, and do or cause to be done all things, necessary, proper or advisable on its part under this Agreement and applicable laws to consummate the Business Combination and the other transactions contemplated hereby as soon as practicable, including preparing and filing as soon as practicable all documentation to effect all necessary notices, reports and other filings and to obtain as soon as practicable all consents, registrations, approvals, permits and authorizations necessary or advisable to be obtained from any third party (including the respective independent accountants of the Company and Parent) and/or any Governmental Entity in order to consummate the Business Combination or any of the other transactions contemplated hereby. This obligation shall include, on the part of Parent, sending a termination letter to Escrow Agent in substantially the form of Exhibit A attached to the Investment Management Trust Agreement by and between Parent and Escrow Agent dated as of December 15, 2005. Subject to applicable laws relating to the exchange of information and the preservation of any applicable attorney-client privilege, work-product doctrine, self-audit privilege or other similar privilege, each of the Company, the Stockholder and Parent shall have the right to review and comment on in advance, and to the extent practicable each will consult the other on, all the information relating to such party, that appear in any filing made with, or written materials submitted to, any third party and/or any Governmental Entity in connection with the Business Combination and the other

Table of Contents

transactions contemplated hereby. In exercising the foregoing right, each of the Company, the Stockholder and Parent shall act reasonably and as promptly as practicable.

(c) Each of the CI Stockholders and Lim shall take such actions and execute all documents necessary, proper and advisable to consummate the transactions contemplated hereby. The foregoing obligations shall include providing all information concerning each of them and/or their ownership of AAI, LLC or any CI company required to be included in the Proxy Statement, 8-Ks, stock exchange listing applications and other filings described in this Agreement.

5.9 *Treatment as a Reorganization*. Neither Parent, the Company, the Stockholder, any of the CI Stockholders, nor Lim shall take any action prior to or following the Business Combination that could reasonably be expected to cause the Merger or any Canada Acquisition to fail to qualify as a reorganization within the meaning of Section 368(a) of the Code.

5.10 *No Parent Common Stock Transactions.* The Stockholder and each of the CI Stockholders shall not, prior to 36 months after the Closing, sell, transfer or otherwise dispose of an interest in any of the shares of Parent Common Stock he, she or it receives as a result of the Business Combination other than as permitted pursuant to the Lock-Up Agreement in the form of *Exhibit D* hereto executed by such Persons concurrently with the execution of this Agreement.

5.11 *Certain Claims*.

(a) As additional consideration for the transactions prescribed hereby, each of the Stockholder, each CI Stockholder and Lim hereby releases and forever discharges, effective as of the Closing Date, each other and the Company and Subsidiaries and their respective directors, officers, employees and agents, from any and all rights, claims, demands, judgments, obligations, liabilities and damages, whether accrued or unaccrued, asserted or unasserted, and whether known or unknown arising out of or resulting from such Person s (i) status as a holder of an equity interest in the Company or any Subsidiary; and (ii) employment, service, consulting or other similar agreement entered into with the Company or any Subsidiary prior to Closing to the extent that the basis for claims under any such agreement that survives the Closing arise prior to the Closing, provided, however, the foregoing shall not release any obligations of such Persons set forth in this Agreement or any other documents executed in connection with the transactions contemplated hereby.

(b) Each party to the (a) stockholders agreement by and among AAI, the Stockholder and Lim in its current form (*AAI Stockholders Agreement*), (b) stockholders agreement by and among any CI company and any of the CI Stockholders in its current form (*CI Stockholders Agreements*) and (c) operating agreement of LLC in its current form (*LLC Operating Agreement* and collectively, with the AAI Stockholders Agreement, CI Stockholders Agreement and any nominee agreements, the *Stockholders Agreements*) hereby irrevocably waives, solely with respect to this Agreement and the transactions and the other documents contemplated hereby, any rights he, she or it may have thereunder that would prevent any Person from executing and delivering this Agreement or performing its obligations hereunder or which would otherwise diminish the rights of any party to this Agreement or prevent the consummation of the Business Combination. Each such Person also hereby agrees that each of the Stockholders Agreements shall be immediately and automatically terminated not later than the date of the Closing and each party thereto hereby automatically waives, effective as of the Closing and only upon consummation of the Business Combination, any and all claims and rights whatsoever that he, she or it may have against any other party thereto with respect to any matter thereunder. Notwithstanding the foregoing, the LLC Operating Agreement shall not so terminate and shall be restated and amended, effective as of the Closing Date, in such form and substance as Parent may determine. All of the waivers, terminations and other actions contemplated by this Section 5.11(b) shall be referred to collectively in this Agreement as the *Stockholders Agreements Waivers*.

Table of Contents

5.12 *No Securities Transactions*. Neither the Company or the Stockholder, nor any of the CI Stockholders or Lim or any of their affiliates, directly or indirectly, shall engage in any transactions involving the securities of Parent prior to the time of the making of a public announcement of the transactions contemplated by this Agreement. The Company shall use its best efforts to require each of its officers, directors, employees, agents and representatives to comply with the foregoing requirement.

5.13 *No Claim Against Trust Fund*. Notwithstanding anything else in this Agreement, the Company, the Stockholder, each of the CI Stockholders and Lim acknowledges that they have read Parent s final prospectus dated December 15, 2005 and understand that Parent has established the Trust Fund for the benefit of Parent s public stockholders and that Parent may disburse monies from the Trust Fund only (a) to Parent s public stockholders in the event they elect to convert their shares into cash in accordance with Parent s Charter Documents and/or the liquidation of Parent or (b) to Parent after it consummates a business combination. The Company, the Stockholder, each of the CI Stockholder and Lim further acknowledge that, if the transactions contemplated by this Agreement, or, upon termination of this Agreement, another business combination, are not consummated by December 15, 2007, Parent will be obligated to return to its stockholders the amounts being held in the Trust Fund. Accordingly, the Company, the Stockholder, each of the CI Stockholders and Lim for themselves and their subsidiaries, affiliated entities, directors, officers, employees, stockholders, representatives, advisors and all other associates and affiliates, hereby waive all rights, title, interest or claim of any kind against Parent and the Merger Sub to collect from the Trust Fund any monies that may be owed to them by Parent or the Merger Sub for any reason whatsoever, including but not limited to a breach of this Agreement by Parent or any negotiations, agreements or understandings with Parent or the Merger Sub (whether in the past, present or future), and will not seek recourse against the Trust Fund at any time for any reason whatsoever. This paragraph will survive this Agreement and will not expire and will not be altered in any way without the express written consent of Parent.

5.14 *Disclosure of Certain Matters*.

(a) Each of Parent, the Company and the Stockholder will provide the others with prompt written notice of any event, development or condition that (a) would cause any of such party s representations and warranties to become untrue or misleading or which may affect its ability to consummate the transactions contemplated by this Agreement, (b) had it existed or been known on the date hereof would have been required to be disclosed under this Agreement, (c) gives such party any reason to believe that any of the conditions set forth in Article VI will not be satisfied, (d) is of a nature that is or may be materially adverse to the operations, prospects or condition (financial or otherwise) of the Company, or (e) would require any amendment or supplement to the Proxy Statement/Prospectus. The parties shall have the obligation to supplement or amend the Company Schedules and Parent Schedules (the *Disclosure Schedules*) being delivered concurrently with the execution of this Agreement and annexed hereto with respect to any matter hereafter arising or discovered which, if existing or known at the date of this Agreement, would have been required to be set forth or described in the Disclosure Schedules. The obligations of the parties to amend or supplement the Disclosure Schedules being delivered herewith shall terminate on the Closing Date. Notwithstanding any such amendment or supplementation, for purposes of Sections 6.2(a), 6.3(a), 7.1(a)(i), 8.1(d) and 8.1(e), the representations and warranties of the parties shall be deemed made as of the date of the December 2006 Agreement with reference to the Disclosure Schedules as they existed at the time of execution of the December 2006 Agreement, other than the Amended Schedules, which shall speak as of the date of this Agreement, subject to changes expressly contemplated by this Agreement or which are set forth in the Disclosure Schedules as they exist on the date of this Agreement.

(b) Each of the CI Stockholders and Lim will provide Parent with prompt written notice of any event, development or condition that would cause any of such Person s representations and warranties to become untrue or misleading or which may affect his, her or its ability to consummate the transactions contemplated by this Agreement,

Table of Contents

5.15 *AMEX Listing*. Parent shall use its best efforts to continue listing of the Parent Common Stock, the Units issued in Parent s initial public offering and the class of warrants included in such Units on the American Stock Exchange. If continued listing is not secured by the Closing, the parties shall continue to use their best efforts after the Closing to obtain such listing. The Company will use its best efforts to provide Parent with information regarding the Company required in connection therewith.

5.16 *Charter Protections; Directors and Officers Liability Insurance*.

(a) All rights to indemnification for acts or omissions occurring through the Closing Date now existing in favor of the current directors and officers of Parent as provided in the Charter Documents of Parent or in any indemnification agreements shall survive the Business Combination and shall continue in full force and effect in accordance with their terms.

(b) For a period of six (6) years after the Closing Date, the Parent and U.S. Surviving Corporation shall cause to be maintained in effect the current policies of directors and officers liability insurance maintained by Parent and the Company, respectively, (or policies of at least the same coverage and amounts containing terms and conditions which are no less advantageous) with respect to claims arising from facts and events that occurred prior to the Closing Date.

(c) If Parent or any of its successors or assigns (i) consolidates with or merges into any other Person and shall not be the continuing or surviving entity of such consolidation or merger, or (ii) transfers or conveys all or substantially all of its properties and assets to any Person, then, in each such case, to the extent necessary, proper provision shall be made so that the successors and assigns of Parent assume the obligations set forth in this Section 5.16.

(d) The provisions of this Section 5.16 are intended to be for the benefit of, and shall be enforceable by, each Person who will have been a director or officer of Parent for all periods ending on or before the Closing Date and may not be changed without the consent of the Appointed Director.

5.17 *Stockholder Obligations*.

(a) The Stockholder, each of the CI Stockholders and Lim shall repay to the Company, on or before the Closing, all direct and indirect indebtedness and other obligations owed by them to the Company, including the indebtedness and other obligations described in *Schedule 2.22* and all other amounts owed by them to the Company.

(b) The Company, the Stockholder, each of the CI Stockholders and Lim, and shall take all necessary actions prior to the Closing to terminate (effective and conditioned up on the Closing) of any and all guarantees furnished by the Company on behalf of any such person, including the Company Guarantees, if any, and as otherwise described in *Schedule 2.22*.

5.18 *Certain Financial Information*. Within 30 days after the end of each month between the date hereof and the earlier of the Closing Date and the date on which this Agreement is terminated, the Company shall deliver to Parent unaudited consolidated financial statements of the Company (including for each of AAI and the CI companies) for such month, including a balance sheet, statement of operations, statement of cash flows and statement of stockholders equity, that are certified as correct and complete by the Chief Executive Officer and Chief Financial Officer of the Company, prepared in accordance with the U.S. GAAP applied on a consistent basis to prior periods (except as may be indicated in the notes thereto) and fairly present in all material respects the financial position of the Company at the date thereof and the results of its operations and cash flows for the period indicated, except that such statements need not contain notes and may be subject to normal adjustments that are not expected to have a Material Adverse Effect on the Company.

5.19 *Access to Financial Information*. The Company will, and will cause its auditors to, (a) continue to provide Parent and its advisors full access to all of the Company s financial information used in the preparation of its Annual Financial Statements and Stub Financial Statements and the financial information furnished pursuant to Section 5.18 hereof and (b) cooperate fully with any reviews performed by Parent or its advisors of any such financial statements or information.

5.20 *Intentionally Omitted*.

5.21 *Intentionally Omitted*.

5.22 *HSR*. If required pursuant to the HSR Act, as promptly as practicable after the date of this Agreement, Parent and the Company shall each prepare and file the notification required of it thereunder in connection with the transactions contemplated by this Agreement and shall promptly and in good faith respond to all information requested of it by the Federal Trade Commission and Department of Justice in connection with such notification and otherwise cooperate in good faith with each other and such Governmental Entities. Parent and the Company shall (a) promptly inform the other of any communication to or from the Federal Trade Commission, the Department of Justice or any other Governmental Entity regarding the transactions contemplated by this Agreement, (b) give the other prompt notice of the commencement of any action, suit, litigation, arbitration, proceeding or investigation by or before any Governmental Entity with respect to such transactions and (c) keep the other reasonably informed as to the status of any such action, suit, litigation, arbitration, proceeding or investigation. Filing fees with respect to the notifications required under the HSR Act shall be shared equally by Parent and the Company.

5.23 *Company Contract Consents*. As soon as practicable after the date hereof and prior to the Closing Date, the Company and the Stockholder shall use best efforts to negotiate with each party to each of the Material Company Contracts and take reasonable action to obtain the consent of each such party required for the assignment of each Company Contract to the Parent or Merger Sub, as appropriate, in each case without change to the terms or provisions of such Company Contract and without the payment of any consideration and to obtain the consent to the Business Combination and related transactions from any third party for which consent is required, including but not limited to all lessors, US Bank, N.A., and C3 Capital Partners, L.P. (collectively, the *Company Contract Consents*). Each Company Contract Consent shall be conditioned upon the consummation of the Business Combination and shall be effective as of the Closing Date.

5.24 *Parent Borrowings*. Through the Closing, Parent shall be allowed to borrow funds from its directors, officers and/or stockholders to meet its reasonable capital requirements, with any such loans to be made only as reasonably required by the operation of Parent in due course on a non-interest bearing basis and repayable at Closing. The proceeds of such loans shall not be used for the payment of salaries, bonuses or other compensation to any of Parent s directors, officers or stockholders.

5.25 *Trust Fund Disbursement*. The Trust Fund shall be dispersed to Parent immediately upon the Closing in an amount not less than $124,043,336, less any amounts required to pay to Lim under Section 5.28 of this Agreement and payments and reserves contemplated hereby, including as follows:

(a) Adequate reserves shall be made by Parent for payments to stockholders of Parent electing to convert their shares of Parent common stock into cash as provided in the Parent s Charter Documents.

(b) All other liabilities of Parent due and owing or incurred at or prior to the Effective Time shall be paid as and when due, including all Parent tax liabilities and the payment at Closing of professional and other fees and expenses related to these transactions, and adequate reserves shall be made against amounts distributed from the Trust Fund therefor.

(c) Parent shall repay at Closing all indebtedness set forth on *Schedule 5.25(c)* in the amounts and to the Persons set forth on such schedule.

(d) As soon as practicable after Closing, Parent shall cause cash bonuses in an aggregate amount of up to $2,500,000 to be paid to certain employees of the Company to be identified on a schedule to be delivered by the Company to Parent at or prior to the Closing.

5.26 *Transfer of LLC Interest.* Immediately prior to the Closing, the Stockholder, Lim and the LLC shall cause all then outstanding membership interests of the LLC to be transferred to AAI (or such other entity that is party to this Agreement as may be selected by Parent) without any consideration being paid by AAI or any other

entity. The LLC membership interests transferred to AAI (or such other designee) shall be free and clear or all Liens and all necessary waivers and consents required to make the transfer as contemplated hereby shall have been obtained by the LLC and the holders of the membership interests.

5.27 *Noncompete*.

(a) For a period of four years from the date of the Closing, none of the Stockholder, any CI Stockholder or Lim shall, directly or indirectly, individually or as an employee, partner, officer, director or shareholder or in any other capacity whatsoever of or for any person, firm, partnership, company or corporation other than Parent, the Company or their respective Subsidiaries or Affiliates:

(i) Own, manage, operate, sell, control or participate in the ownership, management, operation, sales or control of or be connected in any manner, including as an employee, advisor or consultant or similar role, with any business engaged, in the geographical areas referred to in Section 5.27(b) below, in the design, research, development, marketing, sale, branding or licensing of products or services that are substantially similar to or competitive with the business of Parent, the Company or any of their respective Subsidiaries; or

(ii) Recruit, attempt to hire, solicit, or assist others in recruiting or hiring, in or with respect to the geographical areas referred to in Section 5.27(b) below, any person who is an employee of Parent, the Company or any of their respective Subsidiaries or Affiliates or induce or attempt to induce any such employee to terminate his employment with Parent, the Company or any of their respective Subsidiaries or Affiliates.

(b) The geographical areas in which the restrictions provided for in this Section apply include all cities, counties and states of the United States, and all other countries in which Parent, the Company (or any of their respective Subsidiaries or Affiliates) are conducting business at the time in question, whether or not any of Parent, the Company (or such Subsidiary or Affiliate) has an actual physical presence in such location. Each of the Stockholder, each CI Stockholder and Lim acknowledges that (i) the scope and period of restrictions and the geographical area to which the restrictions imposed in this Section applies are fair and reasonable and are reasonably required for the protection of Parent, the Company and their respective Subsidiaries and Affiliates, (ii) this Agreement accurately describes the business to which the restrictions are intended to apply and (iii) the obligations and restrictions provided for herein are an integral part of the consideration motivating Parent to enter into this Agreement.

(c) In addition to, and not in limitation of, the non-competition covenants set forth above in this Section, each of the Stockholder, each CI Stockholder and Lim agrees with Company that for a period of four years from the date of the Closing, he or it will not, either for himself or itself or for any other person or entity, directly or indirectly (other than for Parent, the Company and any of their respective Subsidiaries or Affiliates), solicit business away from, or attempt to sell, license or provide the same or similar products or services as are then provided by Parent, the Company or any Subsidiary or Affiliate thereof to any customer of Parent, the Company or their respective Subsidiaries and Affiliates.

(d) In addition to, and not in limitation of, the non-competition covenants set forth above in this Section, each of the Stockholder, each CI Stockholder and Lim agrees that, for a period of four years from the Closing, he will not, either for himself or itself or for any other person or entity, directly or indirectly, solicit, induce or attempt to induce any executive, employee, consultant or contractor of Parent, the Company or any Subsidiary or Affiliate thereof, to terminate his or her employment or his, her or its services with, Parent, the Company or any Subsidiary or Affiliate thereof or to take employment with another party.

(e) It is the intent of the parties that the provisions of this Section will be enforced to the fullest extent permissible under applicable law. If any particular provision or portion of this Section is adjudicated to be invalid or unenforceable, the Agreement will be deemed amended to revise that provision or portion to the minimum extent necessary to render it enforceable. Such amendment will apply only with respect to the operation of this paragraph in the particular jurisdiction in which such adjudication was made.

Table of Contents

5.28 *Exercise under Lim Option Agreement.* The Company, Parent, Lim and the Stockholder hereby covenant and agree as follows:

(a) It is acknowledged that the Stockholder shall have the right, but not the obligation, to exercise his rights under the Lim Option Agreement prior to Closing of the Business Combination for the Stockholder to consummate the purchase of Lim s Company Capital Stock and Company Membership Interests contemplated thereby (Lim Buy Out).

(b) In the event that the Lim Buy Out is not consummated by the Stockholder prior to Closing for any reason, as part of and in connection with and as a condition to the Merger, Parent shall consummate the Lim Buy Out, rather than Stockholder, by paying to Lim the Lim Payment Amount (as defined) in cash for the surrender of all of his Company Capital Stock and Company Membership Interests and such cash payment shall be deemed part of the consideration paid by Parent for the Merger. Lim shall immediately surrender his Company Capital Stock and Company Membership Interests concurrently with his receipt of the Lim Payment Amount. For the avoidance of doubt, the number of Transaction Shares shall not be reduced by Parent s consummation of the Lim Buy Out pursuant to this Section 5.28(c).

(c) The period under which the Lim Buy Out may occur is hereby extended from May 1, 2007 to the earlier of the consummation of the Lim Buy Out and termination of this Agreement. In consideration of the foregoing, it is hereby agreed that, in the event the Lim Buy Out occurs after May 1, 2007, then, in addition to the $60 million purchase price provided under the Lim Option Agreement for the purchase all of Lim s Company Capital Stock and Company Membership Interests, the buyer thereof shall also pay an additional cash price (*Additional Purchase Price*) on the $60 million purchase price at a rate equal to 20% per annum, compounded monthly, from May 1, 2007 through the date the Lim Buy Out is consummated. The $60 million purchase price plus any Additional Purchase Price shall be referred to as the *Lim Payment Amount*. Each of Lim and the Stockholder hereby agree that the Lim Option Agreement shall be deemed amended and modified as provided in this Section 5.28(c).

(d) Neither Lim nor the Stockholder nor any other party to this Agreement shall agree to any terms in the Lim Buy Out that would adversely affect the other terms of this Agreement or the ability of any party to otherwise consummate the Merger as contemplated by this Agreement.

(e) In connection with the consummation of the Lim Buy Out, the Company and Parent shall cause Lim to be released from any and all personal guarantees made or given by him on behalf of the Company or any Subsidiary thereof and Lim shall otherwise be afforded all releases provided for under the Lim Option Agreement.

(f) Lim agrees that he shall not, until after such time as this Agreement is terminated, sell or transfer any Company Capital Stock or Company Membership Interests to any party other than the Stockholder or Parent as contemplated hereby or cause any Lien to be placed thereon.

(g) Each of the Stockholder and Lim agrees that any default or breach under the Lim Option Agreement that may currently exist or arise after the date hereof and prior to the earlier of the Closing and termination of this Agreement is waived and suspended until such time as the transactions contemplated by this Agreement are consummated or this Agreement is terminated. Each of the Stockholder and Lim agrees that he will not terminate or cause a termination of the Lim Option Agreement prior to the earlier of the Closing and the termination of this Agreement.

(h) Notwithstanding anything to the contrary contained herein or in the Lim Option Agreement and without in any way contradicting, modifying or restricting the nature and extent of the express obligations of a party hereto contained in this Section 5.28 and Lim s right to seek the full extent of damages in the event of a breach, neither Parent nor the Company or any Subsidiary thereof shall be obligated to indemnify Lim or hold him harmless for any liability existing or arising from any circumstances existing prior to the Lim Buy Out.

5.29 [Reserved]

Table of Contents

5.30 *Section 116 Filing.* As soon as practicable after execution of this Agreement, Parent, the Company and the Stockholder shall cause to be prepared and filed all necessary documents and applications necessary to obtain the Section 116 Certificate. Each party shall bear its owns costs in connection with the preparation and filing of the Section 116 Certificate. Any tax liabilities, penalties or interest owed with respect to any taxes or other matters related to the Company s operations or interests in Canada shall be the responsibility of the Company.

5.31 *Employee Matters*. Parent hereby covenants and agrees that immediately following the Closing Date, Parent shall allocate (in accordance with a scheduled delivered to Parent by the Stockholder) an aggregate of 2,710,000 shares of Parent Common Stock available under the Parent Plan for issuance to or for the benefit of those employees of Parent who (i) were employees of the Company as of the date immediately prior to the Closing Date and (ii) are identified by the Stockholder prior to the Closing or no later than the last day of the 90-day period immediately following the Closing Date, which shares shall be issued directly to or for the benefit of such employees pursuant to the terms of the Parent Plan no earlier than the date an effective registration statement on Form S-8 has been filed with respect to the Parent Plan and such shares.

5.32 *Key Person Insurance*. The Company will use commercially reasonable best efforts to secure and maintain key person insurance on the life of the Stockholders for the benefit of the Company in the amount, when aggregated with any existing policies, of $100 million.

ARTICLE VI

CONDITIONS TO THE TRANSACTION

6.1 *Conditions to Obligations of Each Party to Effect the Business Combination*. The respective obligations of each party to this Agreement to affect the Business Combination shall be subject to the satisfaction at or prior to the Closing Date of the following conditions:

(a) *Parent Stockholder Approval*. The Parent Stockholder Approval, the Name Change Amendment and the Capitalization Amendment shall have been duly approved and adopted by the stockholders of Parent by the requisite vote under the laws of the State of Delaware and the Parent Charter Documents and an executed copy of an amendment to Parent s Certificate of Incorporation reflecting the Name Change Amendment and the Capitalization Amendment shall have been filed with the Delaware Secretary of State to be effective as of the Closing.

(b) *Parent Common Stock*. Holders of twenty percent (20%) or more of the shares of Parent Common Stock issued in Parent s initial public offering of securities and outstanding immediately before the Closing shall not have exercised their rights to convert their shares into a pro rata share of the Trust Fund in accordance with Parent s Charter Documents.

(c) *Stock Quotation or Listing*. The Parent Common Stock at the Closing will be listed on the American Stock Exchange or Nasdaq or quoted on the OTC BB and there will be no action or proceeding pending or threatened against Parent to prohibit or terminate such listing or quotation.

(d) *HSR Act*. All specified waiting periods under the HSR Act shall have expired and no Governmental Entity shall have enacted, issued, promulgated, enforced or entered any statute, rule, regulation, executive order, decree, injunction or other order (whether temporary, preliminary or permanent) which is in effect and which has the effect of making the Business Combination illegal or otherwise prohibiting consummation of the Business Combination, substantially on the terms contemplated by this Agreement.

(e) *Lim Buy Out Completion*. The Lim Buy Out shall have been consummated as provided under Section 5.28 and Lim shall have received written assurances from the Company, Parent and the Stockholder that each of their respective covenants, obligations and agreements in favor of Lim that arise from the Lim Buy Out shall be and remain fully enforceable pursuant to their terms and conditions or that same have been satisfied.

(f) *No Order*. No Governmental Entity shall have enacted, issued, promulgated, enforced or entered any statute, rule, regulation, executive order, decree, injunction or other order (whether temporary, preliminary or permanent) which is in effect and which has the effect of making the Business Combination illegal or otherwise prohibiting consummation of the Business Combination, substantially on the terms contemplated by this Agreement.

6.2 *Additional Conditions to Obligations of the Company and Stockholder*. The obligations of the Company and the Stockholder to consummate and affect the Business Combination shall be subject to the satisfaction at or prior to the Closing Date of each of the following conditions, any of which may be waived, in writing, exclusively by the Company and the Stockholder:

(a) *Representations and Warranties*. Each representation and warranty of Parent contained in this Agreement that is (i) qualified as to materiality shall have been true and correct (A) as of the date of the December 2006 Agreement (except with respect to Merger Sub, which shall be true and correct as of the date hereof) and (B) subject to the provisions of the last sentence of Section 5.14, on and as of the Closing Date, with the same force and effect as if made on the Closing Date and (ii) not qualified as to materiality shall have been true and correct (A) as of the date of the December 2006 Agreement (except with respect to Merger Sub, which shall be true and correct as of the date hereof) and (B) subject to the provisions of the last sentence of Section 5.14, on and as of the Closing Date, with the same force and effect as if made on the Closing Date in all material respects as if made on the Closing Date. The Company shall have received a certificate with respect to the foregoing signed on behalf of Parent by an authorized officer of Parent (*Parent Closing Certificate*).

(b) *Agreements and Covenants*. Parent and Merger Sub shall have performed or complied with all agreements and covenants required by this Agreement to be performed or complied with by them on or prior to the Closing Date, except to the extent that any failure to perform or comply (other than a willful failure to perform or comply or failure to perform or comply with an agreement or covenant reasonably within the control of Parent) does not, or will not, constitute a Material Adverse Effect with respect to Parent, and the Parent Closing Certificate shall include a provision to such effect.

(c) *No Litigation*. No action, suit or proceeding shall be pending or threatened before any Governmental Entity which is reasonably likely to (i) prevent consummation of any of the transactions contemplated by this Agreement, (ii) cause any of the transactions contemplated by this Agreement to be rescinded following consummation or (iii) affect materially and adversely or otherwise encumber the title of the shares of Parent Common Stock to be issued by Parent in connection with the Business Combination and no order, judgment, decree, stipulation or injunction to any such effect shall be in effect.

(d) *Consents*. Parent shall have obtained all consents, waivers and approvals required to be obtained by Parent in connection with the consummation of the transactions contemplated hereby, other than consents, waivers and approvals the absence of which, either alone or in the aggregate, could not reasonably be expected to have a Material Adverse Effect on Parent and the Parent Closing Certificate shall include a provision to such effect.

(e) *Material Adverse Effect*. No Material Adverse Effect with respect to Parent shall have occurred since the date of this Agreement.

(f) *SEC Compliance*. Immediately prior to Closing, Parent shall be in compliance with the reporting requirements under the Exchange Act.

(g) *Opinion of Counsel*. Each of the Stockholder and the Company shall have received an opinion from (i) Graubard Miller, Parent s counsel, substantially in the form of *Exhibit E* annexed hereto, and (ii) from Skadden, Arps, Slate, Meagher & Flom LLP (Skadden) or, in the event Skadden does not deliver such opinion, other legal counsel reasonably acceptable to the Stockholder, to the effect that each Canada Acquisition constitutes a reorganization within the meaning of section 368(a) of the Code. Graubard Miller shall be deemed reasonably acceptable to the Stockholder for this purpose.

(h) *Resignations*. The persons currently in the directorships and officers of Parent shall have resigned from all of their positions and offices with Parent necessary to give effect to the Voting Agreement and the other agreements contemplated hereby.

(i) *Trust Fund*. Parent shall have made appropriate arrangements to have the Trust Fund, which shall contain no less than the amount referred to in Section 3.25, dispersed to Parent immediately upon the Closing and in accordance with Section 5.25.

(j) *Stockholder Employment Agreement*. An Employment Agreement in the form of *Exhibit F* hereto between Parent and the Stockholder shall have been executed and delivered at Closing by Parent.

(k) *Voting Agreement*. The Voting Agreement shall be in full force and effect, and the Company s designees thereunder shall have been elected to Parent s Board of Directors.

(l) *Other Deliveries*. At or prior to Closing, Parent shall have delivered to the Company (i) copies of resolutions and actions taken by Parent s board of directors and stockholders in connection with the approval of this Agreement and the transactions contemplated hereunder, and (ii) such other documents or certificates as shall reasonably be required by the Company and its counsel in order to consummate the transactions contemplated hereunder.

6.3 *Additional Conditions to the Obligations of Parent*. The obligations of Parent to consummate and affect the Business Combination shall be subject to the satisfaction at or prior to the Closing Date of each of the following conditions, any of which may be waived, in writing, exclusively by Parent:

(a) *Representations and Warranties*. Each representation and warranty of the Company contained in this Agreement that is (i) qualified as to materiality shall have been true and correct (A) as of the date of the December 2006 Agreement (except with respect to the representations and warranties set forth in Sections 2.1(a), 2.1(b), 2.3(b), 2.15 and 2.22, which shall be true and correct as of the date hereof, giving affect to the Amended Schedules) and (B) subject to the provisions of the last sentence of Section 5.14, on and as of the Closing Date, with the same force and effect as if made on the Closing Date and (ii) not qualified as to materiality shall have been true and correct (A) as of the date of the December 2006 Agreement (except with respect to the representations and warranties set forth in Sections 2.1(a), 2.1(b), 2.3(b), 2.15 and 2.22, which shall be true and correct as of the date hereof, giving affect to the Amended Schedules) and (B) subject to the provisions of the last sentence of Section 5.14, on and as of the Closing Date, in all material respects, with the same force and effect as if made on the Closing Date. Parent shall have received a certificate with respect to the foregoing signed on behalf of the Company by an authorized officer of the Company (*Company Closing Certificate*).

(b) *Agreements and Covenants*. The Company, the Stockholder, each of the CI Stockholders and Lim shall have performed or complied with all agreements and covenants required by this Agreement to be performed or complied with by them at or prior to the Closing Date except to the extent that any failure to perform or comply (other than a willful failure to perform or comply or failure to perform or comply with an agreement or covenant reasonably within the control of the Company) does not, or will not, constitute a Material Adverse Effect on the Company, and the Company Closing Certificate shall include a provision to such effect.

(c) *No Litigation*. No action, suit or proceeding shall be pending or threatened before any Governmental Entity which is reasonably likely to (i) prevent consummation of any of the transactions contemplated by this Agreement, (ii) cause any of the transactions contemplated by this Agreement to be rescinded following consummation or (iii) affect materially and adversely the right of Parent to own, operate or control any of the assets and operations of the Surviving Corporation following the Business Combination and no order, judgment, decree, stipulation or injunction to any such effect shall be in effect.

(d) *Consents*. The Company shall have obtained all consents, waivers, permits and approvals required to be obtained by the Company in connection with the consummation of the transactions contemplated hereby, other than consents, waivers and approvals the absence of which, either alone or in the aggregate,

Table of Contents

could not reasonably be expected to have a Material Adverse Effect on the Company and the Company Closing Certificate shall include a provision to such effect.

(e) *Material Adverse Effect*. No Material Adverse Effect with respect to the Company shall have occurred since the date of this Agreement.

(f) *Opinion of Counsel*. Parent shall have received an opinion in counsel in substantially the form of *Exhibit G* hereto from one or a combination of (i) Buchanan Ingersoll & Rooney PC, special counsel to the Company, and (ii) the Company s Canadian and other general corporate counsels.

(g) *Comfort Letter*. Parent shall have received a comfort letter in the customary form from the Company s independent accountants dated the Closing Date with respect to certain financial statements and other information included in the Proxy Statement.

(h) *Stockholder Obligations*. The Stockholders shall have repaid to the Company, on or before the Closing, all direct and indirect indebtedness and obligations owed by them to the Company, including the indebtedness and other obligations described in *Schedule 2.22* and all other amounts owed by them to the Company.

(i) *Resignations*. The persons currently in the directorships and officers of the Company shall have resigned from all of their positions and offices with the Company necessary to give effect to the Voting Agreement and the other agreements contemplated hereby.

(j) *Derivative Securities*. There shall be outstanding no options, warrants or other derivative securities entitling the holders thereof to acquire shares of Company Capital Stock or other securities of the Company.

(k) *Stockholder Employment Agreement.* The Employment Agreement with the Stockholder shall have been executed and delivered at Closing by the Stockholder.

(l) *Voting Agreement*. The Voting Agreement shall be in full force and effect and the Founders Group s (as defined therein) designees shall have been elected to the Parent s board of directors.

(m) *Cash Bonus Schedule*. The schedule contemplated by Section 5.25(d) shall have been delivered to Parent at or prior to Closing.

(n) *Intentionally Omitted*.

(o) *Intentionally Omitted*.

(p) *Intentionally Omitted*.

(q) *Compliance with Credit Facilities*. On the Closing Date, the Company shall be in full compliance with all of its credit facilities and debt instruments and shall have delivered to Parent written acknowledgment of same from each such facility provider or debt holder.

(r) *Stockholders Agreements Waivers*. The Stockholders Agreements Waivers shall be in full force and effect as of the Closing Date and all necessary actions shall have been taken for all Shareholder Agreements to be automatically terminated upon the closing of the Business Combination, except as otherwise contemplated by Section 5.11(b).

(s) *Transfer of LLC Interests*. The transfer of the membership interests of the LLC in accordance with Section 5.26 of this Agreement shall have been consummated immediately prior to the Closing.

(t) *Lock-up Agreement.* The Lock-up Agreements between Parent and the Stockholder and each CI Stockholder shall be in full force and effect as of the Closing Date.

(u) [Reserved]

(v) *Fairness Opinion*. Parent shall have received an opinion form a qualified investment bank addressed to Parent s board of directors that, as of the date of the opinion, the consideration being given by Parent in the transaction contemplated hereby is fair, from a financial point of view, to the stockholders of

A-46

Table of Contents

Parent and that the fair market value of the Company is at least equal to 80% of the net assets of Parent at the time of the transaction (*Fairness Opinion*).

(w) *Tax Clearance Certificate*. The Section 116 Certificate shall have been obtained or otherwise the provisions of Section 1.6(d)(ii) hereof shall apply.

(x) *Other Deliveries*. At or prior to Closing, the Company shall have delivered to Parent: (i) copies of resolutions and actions taken by the Company s board of directors and stockholders in connection with the adoption and approval of this Agreement and the transactions contemplated hereunder, and (ii) such other documents or certificates as shall reasonably be required by Parent and its counsel in order to consummate the transactions contemplated hereunder.

ARTICLE VII

INDEMNIFICATION

7.1 *Indemnification of Parent*.

(a) Subject to the terms and conditions of this Article VII (including without limitation the limitations set forth in Section 7.4), Parent, the Surviving Corporations and their respective representatives, successors and permitted assigns (the *Parent Indemnitees*) shall be indemnified, defended and held harmless by those Persons who are holders of the Company Capital Stock at the Effective Time, but only to the extent of the Escrow Shares, from and against all Losses asserted against, resulting to, imposed upon, or incurred by any Parent Indemnitee by reason of, arising out of or resulting from:

(i) the inaccuracy or breach of any representation or warranty of the Company contained in or made pursuant to this Agreement, any Schedule or any certificate delivered by the Company to Parent pursuant to this Agreement with respect hereto or thereto in connection with the Closing;

(ii) the non-fulfillment or breach of any covenant or agreement of the Company contained in this Agreement; and

(iii) the matters referred to in Schedule 2.10 of the Company Disclosure Schedule.

(b) As used in this Article VII, the term Losses shall include all losses, liabilities, damages, judgments, awards, orders, penalties, settlements, costs and expenses (including, without limitation, interest, penalties, court costs and reasonable legal fees and expenses) including those arising from any demands, claims, suits, actions, costs of investigation, notices of violation or noncompliance, causes of action, proceedings and assessments whether or not made by third parties or whether or not ultimately determined to be valid. Solely for the purpose of determining the amount of any Losses (and not for determining any breach) for which Parent Indemnitee may be entitled to indemnification pursuant to Article VII, any representation or warranty contained in this Agreement that is qualified by a term or terms such as material, materially, or Material Adverse Effect shall be deemed made or given without such qualification and without giving effect to such words.

7.2 *Indemnification of Third Party Claims*. The indemnification obligations and liabilities under this Article VII with respect to actions, proceedings, lawsuits, investigations, demands or other claims brought against Parent by a Person other than the Company (a *Third Party Claim*) shall be subject to the following terms and conditions:

(a) *Notice of Claim*. Parent, acting through the Appointed Director, will give the Stockholder prompt written notice after receiving written notice of any Third Party Claim or discovering the liability, obligation or facts giving rise to such Third Party Claim (a *Notice of Claim*) which Notice of Third Party Claim shall set forth (i) a brief description of the nature of the Third Party Claim, (ii) the total amount of the actual out-of-pocket Loss or the anticipated potential Loss (including any costs or expenses which have been or

may be reasonably incurred in connection therewith), and (iii) whether such Loss may be covered (in whole or in part) under any insurance and the estimated amount of such Loss which may be covered under such insurance, and the Stockholder shall be entitled to participate in the defense of Third Party Claim at its expense.

(b) *Defense.* The Stockholder shall have the right, at its option (subject to the limitations set forth in subsection 7.2(c) below) and at its own expense, by written notice to Parent, to assume the entire control of, subject to the right of Parent to participate (at its expense and with counsel of its choice) in, the defense, compromise or settlement of the Third Party Claim as to which such Notice of Claim has been given, and shall be entitled to appoint a recognized and reputable counsel reasonably acceptable to Parent to be the lead counsel in connection with such defense. If the Stockholder is permitted and elects to assume the defense of a Third Party Claim:

(i) the Stockholder shall diligently and in good faith defend such Third Party Claim and shall keep Parent reasonably informed of the status of such defense; provided, however, that Parent shall have the right to approve any settlement, which approval shall not be unreasonably delayed, withheld or conditioned; and

(ii) Parent shall cooperate fully in all respects with the Stockholder in any such defense, compromise or settlement thereof, including, without limitation, the selection of counsel, and Parent shall make available to the Stockholder all pertinent information and documents under its control.

(c) *Limitations of Right to Assume Defense.* The Stockholder shall not be entitled to assume control of such defense if (i) the Third Party Claim relates to or arises in connection with any criminal proceeding, action, indictment, allegation or investigation; (ii) the Third Party Claim seeks an injunction or equitable relief against Parent; or (iii) there is a reasonable probability that a Third Party Claim may materially and adversely affect Parent other than as a result of money damages or other money payments.

(d) *Other Limitations.* Failure to give prompt Notice of Claim or to provide copies of relevant available documents or to furnish relevant available data shall not constitute a defense (in whole or in part) to any Third Party Claim by Parent against the Stockholder and shall not affect the Stockholder s duty or obligations under this Article VII, except to the extent (and only to the extent that) such failure shall have adversely affected the ability of the Stockholder to defend against or reduce its liability or caused or increased such liability or otherwise caused the damages for which the Stockholder is obligated to be greater than such damages would have been had Parent given the Stockholder prompt notice hereunder. So long as the Stockholder is defending any such action actively and in good faith, Parent shall not settle such action. Parent shall make available to the Stockholder all relevant records and other relevant materials required by them and in the possession or under the control of Parent, for the use of the Stockholder and its representatives in defending any such action, and shall in other respects give reasonable cooperation in such defense.

(e) *Failure to Defend.* If the Stockholder, promptly after receiving a Notice of Claim, fails to defend such Third Party Claim actively and in good faith, Parent will (upon further written notice) have the right to undertake the defense, compromise or settlement of such Third Party Claim as it may determine in its reasonable discretion, provided that the Stockholder shall have the right to approve any settlement, which approval will not be unreasonably delayed, withheld or conditioned.

(f) *Parent s Rights.* Anything in this Section 7.2 to the contrary notwithstanding, the Stockholder shall not, without the written consent of Parent, settle or compromise any action or consent to the entry of any judgment which does not include as an unconditional term thereof the giving by the claimant or the plaintiff to Parent of a full and unconditional release from all liability and obligation in respect of such action without any payment by Parent.

(g) *Stockholder Consent*. Unless the Stockholder has consented to a settlement of a Third Party Claim, the amount of the settlement shall not be a binding determination of the amount of the Loss and such amount shall be determined in accordance with the provisions of the Escrow Agreement.

Table of Contents

7.3 *Insurance Effect*. To the extent that any Losses that are subject to indemnification pursuant to this Article VII are covered by insurance, Parent shall use best efforts to obtain the maximum recovery under such insurance; provided that Parent shall nevertheless be entitled to bring a claim for indemnification under this Article VII in respect of such Losses and the time limitations set forth in Section 7.4 hereof for bringing a claim of indemnification under this Agreement shall be tolled during the pendency of such insurance claim. The existence of a claim by Parent for monies from an insurer or against a third party in respect of any Loss shall not, however, delay any payment pursuant to the indemnification provisions contained herein and otherwise determined to be due and owing by the Stockholder. If Parent has received the payment required by this Agreement from the Stockholder in respect of any Loss and later receives proceeds from insurance or other amounts in respect of such Loss, then it shall hold such proceeds or other amounts in trust for the benefit of the Stockholder and shall pay to the Stockholder, as promptly as practicable after receipt, a sum equal to the amount of such proceeds or other amount received, up to the aggregate amount of any payments received from the Stockholder pursuant to this Agreement in respect of such Loss. Notwithstanding any other provisions of this Agreement, it is the intention of the parties that no insurer or any other third party shall be (i) entitled to a benefit it would not be entitled to receive in the absence of the foregoing indemnification provisions, or (ii) relieved of the responsibility to pay any claims for which it is obligated.

7.4 *Limitations on Indemnification*.

(a) *Survival; Time Limitation.* The representations, warranties, covenants and agreements in this Agreement or in any writing delivered by the Company to Parent in connection with this Agreement (including the certificate required to be delivered by the Company pursuant to Section 6.3(a)) shall survive the Closing until the expiration of the Escrow Period.

(b) Any claim made by a party hereunder shall be preserved despite the subsequent expiration of the Escrow Period and any claim set forth in a Notice of Claim sent prior to the expiration of the Escrow Period shall survive until final resolution thereof. Except as set forth in the immediately preceding sentence, no claim for indemnification under this Article VII shall be brought after the end of the Escrow Period.

(c) *Deductible.* No amount shall be payable under Article VII unless and until the aggregate amount of all indemnifiable Losses otherwise payable exceeds $250,000 (the *Deductible*), in which event the amount payable shall include all amounts included in the Deductible and all future amounts that become payable under Section 7.1 from time to time thereafter.

(d) *Aggregate Amount Limitation.* The aggregate liability for Losses pursuant to Section 7.1 shall not in any event exceed the Escrow Shares and Parent shall have no claim against the Company s stockholders other than for the Escrow Shares (and any proceeds of the shares or distributions with respect to the Escrow Shares).

7.5 *Exclusive Remedy*. Parent, on behalf of itself and all other Parent Indemnitees, hereby acknowledges and agrees that, from and after the Closing, its sole remedy with respect to any and all claims for money damages arising out of or relating to this Agreement shall be pursuant and subject to the requirements of the indemnification provisions set forth in this Article VII. Notwithstanding any of the foregoing, nothing contained in this Article VII shall in any way impair, modify or otherwise limit Parent s or the Company s right to bring any claim, demand or suit against the other party based upon such other party s actual fraud or intentional or willful misrepresentation or omission, it being understood that a mere breach of a representation and warranty, without intentional or willful misrepresentation or omission, does not constitute fraud.

7.6 *Adjustment to Transaction Consideration*. Amounts paid for indemnification under Article VII shall be deemed to be an adjustment to the value of the shares of Parent Common Stock issued by Parent as a result of the Business Combination, except as otherwise required by Law.

7.7 *Stockholder Capacities; Application of Escrow Shares*. The parties acknowledge that the Stockholder s obligations under this Article VII are solely as a representative of the Company s stockholders in the manner set forth in the Escrow Agreement with respect to the obligations to indemnify Parent under this Article VII and that

the Stockholder shall have no personal responsibility for any expenses incurred by him in such capacity and that all payments to Parent as a result of such indemnification obligations shall be made solely from, and to the extent of, the Escrow Shares. The parties further acknowledge that all actions to be taken by Parent pursuant to this Article VII shall be taken on its behalf by the Appointed Director in accordance with the provisions of the Escrow Agreement. The Escrow Agent, pursuant to the Escrow Agreement after the Closing, may apply all or a portion of the Escrow Shares to satisfy any claim for indemnification pursuant to this Article VII. The Escrow Agent will hold the remaining portion of the Escrow Shares until final resolution of all claims for indemnification or disputes relating thereto.

ARTICLE VIII

TERMINATION

8.1 *Termination*. This Agreement may be terminated at any time prior to the Closing:

(a) by mutual written agreement of Parent and the Company at any time;

(b) by either Parent or the Company if the Business Combination shall not have been consummated by December 15, 2007 for any reason; provided, however, that the right to terminate this Agreement under this Section 8.1(b) shall not be available to any party whose action or failure to act has been a principal cause of or resulted in the failure of the Business Combination to occur on or before such date and such action or failure to act constitutes a breach of this Agreement;

(c) by either Parent or the Company if a Governmental Entity shall have issued an order, decree, judgment or ruling or taken any other action, in any case having the effect of permanently restraining, enjoining or otherwise prohibiting the Business Combination, which order, decree, ruling or other action is final and nonappealable;

(d) by the Company, upon a material breach of any representation, warranty, covenant or agreement on the part of Parent set forth in this Agreement, or if any representation or warranty of Parent shall have become untrue, in either case such that the conditions set forth in Article VI would not be satisfied as of the time of such breach or as of the time such representation or warranty shall have become untrue, provided, that if such breach by Parent is curable by Parent prior to the Closing Date, then the Company may not terminate this Agreement under this Section 8.1(d) for thirty (30) days after delivery of written notice from the Company to Parent of such breach, provided Parent continues to exercise best efforts to cure such breach (it being understood that the Company may not terminate this Agreement pursuant to this Section 8.1(d) if it shall have materially breached this Agreement or if such breach by Parent is cured during such thirty (30)-day period);

(e) by Parent, upon a material breach of any representation, warranty, covenant or agreement on the part of the Company set forth in this Agreement, or if any representation or warranty of the Company shall have become untrue, in either case such that the conditions set forth in Article VI would not be satisfied as of the time of such breach or as of the time such representation or warranty shall have become untrue, provided, that if such breach is curable by the Company prior to the Closing Date, then Parent may not terminate this Agreement under this Section 8.1(e) for thirty (30) days after delivery of written notice from Parent to the Company of such breach, provided the Company continues to exercise best efforts to cure such breach (it being understood that Parent may not terminate this Agreement pursuant to this Section 8.1(e) if it shall have materially breached this Agreement or if such breach by the Company is cured during such thirty (30)-day period); or

(f) by either Parent or the Company, if, at the Special Meeting (including any adjournments thereof), this Agreement and the transactions contemplated thereby shall fail to be approved and adopted by the affirmative vote of the holders of Parent Common Stock required under Parent s certificate of incorporation, or the holders of 20% or more of the number of shares of Parent Common Stock issued in Parent s initial

public offering and outstanding as of the date of the record date of the Special Meeting exercise their rights to convert the shares of Parent Common Stock held by them into cash in accordance with Parent s certificate of incorporation.

8.2 *Notice of Termination; Effect of Termination*. Any termination of this Agreement under Section 8.1 above will be effective immediately upon (or, if the termination is pursuant to Section 8.1(d) or Section 8.1(e) and the proviso therein is applicable, thirty (30) days after) the delivery of written notice of the terminating party to the other parties hereto. In the event of the termination of this Agreement as provided in Section 8.1, this Agreement shall be of no further force or effect and the Business Combination shall be abandoned, except for and subject to the following: (i) Sections 5.6, 5.13, 8.2 and 8.3 and Article X (General Provisions) shall survive the termination of this Agreement, and (ii) nothing herein shall relieve any party from liability for any breach of this Agreement, including a breach by a party electing to terminate this Agreement pursuant to Section 8.1(b) if such party s action or failure to act constituted a principal cause of or resulted in the failure of the Business Combination to occur on or before the date stated therein.

8.3 *Fees and Expenses*. All fees and expenses incurred in connection with this Agreement and the transactions contemplated hereby shall be paid by the party incurring such expenses whether or not the Business Combination is consummated.

ARTICLE IX

DEFINED TERMS

Terms defined in this Agreement are organized alphabetically as follows, together with the Section and, where applicable, paragraph, number in which definition of each such term is located:

AAA	Section 10.12
AAI	Header
AAI Stockholders Agreement	Section 5.11(b)
Acquisition Transaction	Section 4.2(a)
Additional Purchase Price	Section 5.28(c)
Affiliate	Section 10.2(f)
Agreement	Header
Amended Schedules	Header
AMEX	Section 3.23
Applicable Corporate Laws	Recital A
Appointment Director	Section 1.13
Approvals	Section 2.1(a)
Annual Financial Statements	Section 2.7(a)
Blue Sky Laws	Section 1.12(c)
Business Combination	Section 1.1(b)
Canada Acquisition	Section 1.1(b)
Canadian Allocation	Section 1.6(d)(ii)
Canadian Escrow Shares	Section 1.6(d)(iv)
Canadian Shares	Section 1.6(d)(ii)
Canadian Tax Act	Section 1.6(d)(i)
Capitalization Amendment	Section 5.1(b)
Charter Documents	Section 2.1(a)
CI	Header
CI companies	Header
CI Stockholders	Header

Table of Contents

CI Stockholders Agreement	Section 5.11(b)
CI Stockholders Signature Page	Section 2.3(b)
Closing	Section 1.2
Closing Date	Section 1.2
Closing Date Net Debt	Section 1.5(b)(i)
Closing Date Net Debt Statement	Section 1.5(b)(iv)
Closing Form 8-K	Section 5.4(b)
Closing Press Release	Section 5.4(b)
Code	Recital E
Comfort Letter	Section 6.3(g)
Company	Header
Company Certificates	Section 1.6(a)
Company Closing Certificate	Section 6.3(a)
Company Capital Stock	Section 1.5(a)
Company Contracts	Section 2.19(a)
Company Contract Consents	Section 5.21
Company Intellectual Property	Section 2.18
Company Membership Interests	Section
Company Products	Section 2.18
Company Registered Intellectual Property	Section 2.18
Company Schedule	Article II Preamble
Company Stock Options	Section 2.3(c)
Company Warrants	Section 2.3(c)
Copyrights	Section 2.18
Corporate Records	Section 2.1(c)
December 2006 Agreement	Header
Deductible	Section 7.4(c)
DGCL	Section 5.1(b)
Disclosure Schedules	Section 5.14(a)
Distribution Date	Section 1.15
Due Date	Section 1.6(d)(v)
Effective Time	Section 1.2
Employment Agreements	Section 6.2(j)
Environmental Law	Section 2.16(b)
Escrow Agent	Section 1.11
Escrow Agreement	Section 1.11
Escrow Period	Section 1.11
Escrow Shares	Section 1.5(a)
Exchange Act	Section 1.12(c)
Governmental Action/Filing	Section 2.21(c)
Governmental Entity	Section 1.12(c)
HSR Act	Section 2.5(b)
Hazardous Substance	Section 2.16(c)
Indemnity Shares	Section 1.5(a)
Insider	Section 2.19(a)(i)
Insurance Policies	Section 2.20
Intellectual Property	Section 2.18
knowledge	Section 10.2(d)
Legal Requirements	Section 10.2(b)
LLC	Header
LLC Operating Agreement	Section 5.11(b)
Lien	Section 10.2(e)

Table of Contents

Lim	Header
Lim Buy Out	Section 5.28(a)
Lim Option Agreement	Section 2.26
Lim Payment Amount	Section 5.28(c)
Losses	Section 7.1(b)
Material Adverse Effect	Section 10.2(a)
Material Company Contracts	Section 2.19(a)
Merger	Section 1.1(a)
Merger Sub	Header
Name Change Amendment	Section 5.1(b)
Net Debt	Section 1.5(c)(iii)
Net Debt Transaction Share Reduction	Section 1.5(c)(ii)
Notice of Claim	Section 7.2(a)
Parent	Header
Parent Closing Certificate	Section 6.2(a)
Parent Common Stock	Section 1.5(a)
Parent Contracts	Section 3.19(a)
Parent Convertible Securities	Section 3.3(b)
Parent Indemnitees	Section 7.1(a)
Parent Plan	Section 5.1(b)
Parent Preferred Stock	Section 3.3(a)
Parent SEC Reports	Section 3.7(a)
Parent Schedule	Article III Preamble
Parent Stock Options	Section 3.3(b)
Parent Stockholder Approval	Section 5.1(b)
Parent Warrants	Section 3.3(b)
Patents	Section 2.18
Periodic Net Debt Statement	Section 1.5(b)(iv)
Person	Section 10.2(c)
Personal Information	Section 2.27(a)
Personal Property	Section 2.14(b)
Plan/Plans	Section 2.11(a)
Press Release	Section 5.4(a)
Privacy Laws	Section 2.27(a)
Privacy Policy	Section 2.27(b)
Proxy Statement	Section 5.1(b)
Recipient Party	Section 1.6(d)(i)
Registered Intellectual Property	Section 2.18
Registration Rights Agreement	Section 1.14
Returns	Section 2.15(b)(i)
Section 116 Certificate	Section 1.6(d)(i)
Securities Act	Section 1.12
Signing Form 8-K	Section 5.4(a)
Special Meeting	Section 5.1(b)
Stockholders Agreement	Section 5.11(b)
Stockholders Agreements Waivers	Section 5.11(b)
Stub Financial Statements	Section 2.7(b)
Stub Period Tax Amounts	Section 1.15
Stockholder	Header
Subsidiary/Subsidiaries	Section 2.2(a)
Surviving Corporations	Section 1.1(b)
Tax/Taxes	Section 2.15(a)

Table of Contents

Third Party Claim	Section 7.2
Trademarks	Section 2.18
Transaction Certificates	Section 1.2
Transaction Consideration	Section 1.5(a)
Transaction Shares	Section 1.5(a)
Trust Fund	Section 3.25
U.S. GAAP	Section 2.7(a)
U.S. Surviving Corporation	Section 1.1(a)

ARTICLE X

GENERAL PROVISIONS

10.1 *Notices*. All notices and other communications hereunder shall be in writing and shall be deemed given if delivered personally or by commercial delivery service, or sent via telecopy (receipt confirmed) to the parties at the following addresses or telecopy numbers (or at such other address or telecopy numbers for a party as shall be specified by like notice):

if to Parent, to:

Endeavor Acquisition Corp.

590 Madison Avenue

21st Floor

New York, New York 10022

Attention: Jonathan Ledecky

212-409-2409 telephone

212-409-2407 telecopy

with a copy to:

David Alan Miller, Esq.

Graubard Miller

405 Lexington Avenue

New York, New York 10174-1901

212-818-8661 telephone

212-818-8881 telecopy

if to the Company or Stockholder, to:

American Apparel Inc.

747 Warehouse Street

Los Angeles, California 90021

Attention: Dov Charney

213-488-0226 telephone

213-488-0334 telecopy

with a copy to:

Buchanan Ingersoll & Rooney PC

One Chase Manhattan Plaza

35th Floor

New York, New York 10005-1417

Attention: Brian North, Esq.

212-440-4400 telephone

212-440-4401 telecopy

Table of Contents

and

Skadden, Arps, Slate, Meagher & Flom LLP

300 South Grand Avenue

Suite 3400

Los Angeles, California 90071

Attention: Jeffrey H. Cohen, Esq.

David C. Eisman, Esq.

213-687-5000 telephone

213-687-5600 telecopy

10.2 *Interpretation*. The definitions of the terms herein shall apply equally to the singular and plural forms of the terms defined. Whenever the context shall require, any pronoun shall include the corresponding masculine, feminine and neuter forms. When a reference is made in this Agreement to an Exhibit or Schedule, such reference shall be to an Exhibit or Schedule to this Agreement unless otherwise indicated. When a reference is made in this Agreement to Sections or subsections, such reference shall be to a Section or subsection of this Agreement. Unless otherwise indicated the words include, includes and including when used herein shall be deemed in each case to be followed by the words without limitation. The table of contents and headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. When reference is made herein to the business of an entity, such reference shall be deemed to include the business of all direct and indirect Subsidiaries of such entity. Reference to the Subsidiaries of an entity shall be deemed to include all direct and indirect Subsidiaries of such entity. For purposes of this Agreement:

(a) the term *Material Adverse Effect* when used in connection with an entity means any change, event, violation, inaccuracy, circumstance or effect, individually or when aggregated with other changes, events, violations, inaccuracies, circumstances or effects, that is materially adverse to the business, assets (including intangible assets), revenues, financial condition, prospects or results of operations of such entity, it being understood that none of the following alone or in combination shall be deemed, in and of itself, to constitute a Material Adverse Effect: (i) changes attributable to the public announcement or pendency of the transactions contemplated hereby, (ii) changes in general national or regional economic conditions, or (iii) any SEC rulemaking requiring enhanced disclosure of reverse merger transactions with a public shell;

(b) the term *Legal Requirements* means any federal, state, local, municipal, foreign or other law, statute, constitution, principle of common law, resolution, ordinance, code, edict, decree, rule, regulation, ruling or requirement issued, enacted, adopted, promulgated, implemented or otherwise put into effect by or under the authority of any Governmental Entity and all requirements set forth in applicable Company Contracts or Parent Contracts;

(c) the term *Person* shall mean any individual, corporation (including any non-profit corporation), general partnership, limited partnership, limited liability partnership, joint venture, estate, trust, company (including any limited liability company or joint stock company), firm or other enterprise, association, organization, entity or Governmental Entity;

(d) the term *knowledge* means actual knowledge or awareness, after due inquiry, as to a specified fact or event of a Person that is an individual or of an executive officer or director of a Person that is a corporation or of a Person in a similar capacity of an entity other than a corporation;

(e) the term *Lien* means any mortgage, pledge, security interest, encumbrance, lien, restriction or charge of any kind (including, without limitation, any conditional sale or other title retention agreement or lease in the nature thereof, any sale with recourse against the seller or any Affiliate of the seller, or any agreement to give any security interest);

(f) the term *Affiliate* means, as applied to any Person, any other Person directly or indirectly controlling, controlled by or under direct or indirect common control with, such Person. For purposes of this definition, control (including with correlative meanings, the terms controlling, controlled by and

A-55

Table of Contents

under common control with), as applied to any Person, means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of such Person, whether through the ownership of voting securities, by contract or otherwise; and

(g) all monetary amounts set forth herein are referenced in United States dollars, unless otherwise noted.

10.3 *Counterparts; Facsimile Signatures*. This Agreement and each other document executed in connection with the transactions contemplated hereby, and the consummation thereof, may be executed in one or more counterparts, all of which shall be considered one and the same document and shall become effective when one or more counterparts have been signed by each of the parties and delivered to the other party, it being understood that all parties need not sign the same counterpart. Delivery by facsimile to counsel for the other party of a counterpart executed by a party shall be deemed to meet the requirements of the previous sentence.

10.4 *Entire Agreement; Third Party Beneficiaries*. This Agreement and the documents and instruments and other agreements among the parties hereto as contemplated by or referred to herein, including the Exhibits and Schedules hereto (a) constitute the entire agreement among the parties with respect to the subject matter hereof and supersede all prior agreements and understandings, both written and oral, among the parties with respect to the subject matter hereof, and (b) are not intended to confer upon any other person any rights or remedies hereunder (except as specifically provided in this Agreement).

10.5 *Severability*. In the event that any provision of this Agreement, or the application thereof, becomes or is declared by a court of competent jurisdiction to be illegal, void or unenforceable, the remainder of this Agreement will continue in full force and effect and the application of such provision to other persons or circumstances will be interpreted so as reasonably to effect the intent of the parties hereto. The parties further agree to replace such void or unenforceable provision of this Agreement with a valid and enforceable provision that will achieve, to the extent possible, the economic, business and other purposes of such void or unenforceable provision.

10.6 *Other Remedies; Specific Performance*. Except as otherwise provided herein, any and all remedies herein expressly conferred upon a party will be deemed cumulative with and not exclusive of any other remedy conferred hereby, or by law or equity upon such party, and the exercise by a party of any one remedy will not preclude the exercise of any other remedy. The parties hereto agree that irreparable damage would occur in the event that any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the parties shall be entitled to seek an injunction or injunctions to prevent breaches of this Agreement and to enforce specifically the terms and provisions hereof in any court of the United States or any state having jurisdiction, this being in addition to any other remedy to which they are entitled at law or in equity. The parties further acknowledge that the Company and its assets, business and equity securities are unique and therefore, in the event of the Company s failure to consummate the Business Combination for any reason other than Parent s or Merger Sub breach hereunder, Parent shall have the right to seek equitable relief hereunder, including specific performance.

10.7 *Governing Law*. This Agreement shall be governed by and construed in accordance with the law of the State of Delaware regardless of the law that might otherwise govern under applicable principles of conflicts of law thereof.

10.8 *Rules of Construction*. The parties hereto agree that they have been represented by counsel during the negotiation and execution of this Agreement and, therefore, waive the application of any law, regulation, holding or rule of construction providing that ambiguities in an agreement or other document will be construed against the party drafting such agreement or document.

10.9 *Assignment*. No party may assign either this Agreement or any of its rights, interests, or obligations hereunder without the prior written approval of the other parties. Subject to the first sentence of this Section 10.9, this Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective

successors and permitted assigns. Notwithstanding the foregoing, Parent may assign all or any portion of its rights under this Agreement to any of its affiliates (whether currently existing or created hereafter), but no such assignment shall relieve Parent of its obligations hereunder.

10.10 *Amendment*. This Agreement may be amended by the parties hereto at any time by execution of an instrument in writing signed on behalf of each of the parties.

10.11 *Extension; Waiver*. At any time prior to the Closing, any party hereto may, to the extent legally allowed, (i) extend the time for the performance of any of the obligations or other acts of the other parties hereto, (ii) waive any inaccuracies in the representations and warranties made to such party contained herein or in any document delivered pursuant hereto and (iii) waive compliance with any of the agreements or conditions for the benefit of such party contained herein. Any agreement on the part of a party hereto to any such extension or waiver shall be valid only if set forth in an instrument in writing signed on behalf of such party. Delay in exercising any right under this Agreement shall not constitute a waiver of such right.

10.12 *Arbitration*. Any disputes or claims arising under or in connection with this Agreement or the transactions contemplated hereunder shall be resolved by binding arbitration. Notice of a demand to arbitrate a dispute by either party shall be given in writing to the other at their last known address. Arbitration shall be commenced by the filing by a party of an arbitration demand with the American Arbitration Association (*AAA*) in its office in New York City. The arbitration and resolution of the dispute shall be resolved by a single arbitrator appointed by the AAA pursuant to AAA rules. The arbitration shall in all respects be governed and conducted by applicable AAA rules, and any award and/or decision shall be conclusive and binding on the parties. The arbitration shall be conducted in New York City. The arbitrator shall supply a written opinion supporting any award, and judgment may be entered on the award in any court of competent jurisdiction. Each party shall pay its own fees and expenses for the arbitration, except that any costs and charges imposed by the AAA and any fees of the arbitrator for his services shall be assessed against the losing party by the arbitrator. In the event that preliminary or permanent injunctive relief is necessary or desirable in order to prevent a party from acting contrary to this Agreement or to prevent irreparable harm prior to a confirmation of an arbitration award, then either party is authorized and entitled to commence a lawsuit solely to obtain equitable relief against the other pending the completion of the arbitration in a court having jurisdiction over the parties. Each party hereby consents to the exclusive jurisdiction of the federal and state courts located in the State of New York, New York County, for such purpose. All rights and remedies of the parties shall be cumulative and in addition to any other rights and remedies obtainable from arbitration.

10.13 *Currency*. All references to currency amounts in this Agreement shall mean United States dollars.

10.14 *Waiver and Release*. Each party hereto hereby waives any breach (or alleged breach) by any other party of, and any failure (or alleged failure) of a party to comply with, prior to the date of this Agreement (as amended and restated), any representation, warranty or covenant originally set forth in the December 2006 Agreement that has been deleted from this Agreement or any representation, warranty or covenant originally set forth in the December 2006 Agreement that has been updated or modified by this Agreement. To the fullest extent permitted by law, each of the parties hereto hereby waives and releases any claims that it may have against another party with respect to, and any Losses that have been or may be asserted against, resulting to, imposed upon or incurred by any Parent Indemnitee by reason of, arising out of or resulting from or in connection with any such breach (or alleged breach) or failure (or alleged failure) to comply. Notwithstanding anything to the contrary contained herein, nothing herein shall be deemed to constitute a waiver of any other representation, warrant or covenant originally contained in the December 2006 Agreement or a waiver of any breach occurring on or after the date hereof.

[The remainder of this page has been intentionally left blank.]

Table of Contents

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date first written above.

ENDEAVOR ACQUISITION CORPORATION

By: /s/ Jon Ledecky
Name and Title

AAI ACQUISITION LLC

By: /s/ Jon Ledecky
Name and Title

AMERICAN APPAREL, INC.

By: /s/ Dov Charney
Name and Title

AMERICAN APPAREL, LLC

By: /s/ Dov Charney
Name and Title

AMERICAN APPAREL CANADA RETAIL INC.

By: /s/ Dov Charney
Name and Title

AMERICAN APPAREL CANADA WHOLESALE INC.

By: /s/ Dov Charney
Name and Title

/s/ Dov Charney
DOV CHARNEY

SEE SEPARATE SIGNATURE PAGES FOR SIGNATURE OF EACH OF THE CI STOCKHOLDERS AND LIM

THE SIGNATURES OF THE CI STOCKHOLDERS (AND THE RELATED NOMINEES) CONSTITUTE THEIR RESPECTIVE INDIVIDUAL SIGNATURES AS WELL AS THEIR SIGNATURES ON BEHALF OF THE CI COMPANIES

Table of Contents

SANG HO LIM SIGNATURE PAGE

The Signature of the Person below constitutes his agreement only to Sections 1.1(a), 1.5(a), 1.6, 1.7, 1.8, 1.9, 1.10 1.12(a), 1.12(c,) 1.15, 2.3(a), 2.3(c), 2.4(a), 2.4(c), 2.5(b), 2.24, 4.1(f), 4.2, 5.6, 5.8(c), 5.9, 5.11, 5.12, 5.13, 5.14(b), 5.17, 5.26, 5.27,5.28, Article VIII, Article IX and Article X.

/s/ Sang Ho Lim
SANG HO LIM

A-59

Table of Contents

OTHER CI STOCKHOLDER SIGNATURE PAGE

The Signature of each Person below constitutes his, her or its only to Sections 1.1(b), 1.5(a), 1.5(b), 1.6, 1.7, 1.8, 1.9, 1.12, 2.3(b), 2.4(a), 2.4(c), 2.24, 4.1(f), 4.2, 5.6, 5.8(c), 5.9, 5.10, 5.11, 5.12, 5.13, 5.14(b), 5.17, Article VIII, Article IX and Article X.

/s/ Dov Charney
DOV CHARNEY
(in his capacity as a CI Stockholder)

/s/ Morris Charney
MORRIS CHARNEY

Table of Contents

SCHEDULE A

THE CI COMPANIES

Name of Company	Jurisdiction Formed/Law of Formation	Beneficial Holder s Name
American Apparel Canada Retail Inc.	Canada Business Corporations Act	Dov Charney
American Apparel Canada Wholesale Inc.	Canada Business Corporations Act	Dov Charney

A-61

Table of Contents

SCHEDULE 1.2

APPLICABLE JURISDICTIONS AND FILINGS

Company	**Jurisdiction of Organization**	**Transaction Document to be Filed**
American Apparel, Inc.	California	Articles of Merger and any applicable filing required under California law.
American Apparel, LLC	California	Any applicable publication or filing required under California law.
American Apparel Canada Retail Inc.	British Columbia, Alberta, Ontario, Quebec, Nova Scotia	Section 116 Certificate Application
American Apparel Canada Wholesale Inc.	Quebec	Section 116 Certificate Application

A-62

Table of Contents

SCHEDULE 1.5(a)

ALLOCATION OF TRANSACTION SHARES

[*to be updated prior to Closing pursuant to Section 1.5(a)*]

SCHEDULE 2

COMPANY SCHEDULE

(Information Furnished Separately)

Schedule 2.1	Organization and Qualification*
Schedule 2.2	Subsidiaries*
Schedule 2.3	Capitalization*
Schedule 2.5	Required Consents**
Schedule 2.6	Compliance***
Schedule 2.7	Financial Statements (Included elsewhere in proxy statement.)
Schedule 2.8	No Undisclosed Liabilities***
Schedule 2.9	Absence of Certain Changes or Events***
Schedule 2.10	Litigation**
Schedule 2.11	Employee Benefit Plans*
Schedule 2.12	Labor Matters**
Schedule 2.13	Restrictions on Business Activities***
Schedule 2.14	Title to Property**
Schedule 2.15	Taxes***
Schedule 2.16	Environmental Matters***
Schedule 2.17	Brokers; Third Party Expenses***
Schedule 2.18	Intellectual Property**
Schedule 2.19	Agreements, Contracts and Commitments**
Schedule 2.20	Insurance*
Schedule 2.21	Governmental Actions/Filings**
Schedule 2.22	Interested Party Transactions**
Schedule 2.25	Product Liability; Product Recalls***

* Information not material. Schedule omitted.
** Schedule included in Annex A.
*** No exceptions on schedule. Schedule omitted.

Table of Contents

SCHEDULE 2.5(b)

NO CONFLICT; REQUIRED FILLINGS AND CONSENTS

Leases and bank lines.

Table of Contents

SCHEDULE 2.10(a)

LITIGATION DISCLOSURES

OPEN LITIGATION MATTERS

Matter	**Date Filed**	**Brief Description of Case**	**Current Status**
Los Angeles County Metropolitan Transportation Authority v. VCC Alameda *et al*.	April 2004	Eminent Domain regarding off-site parking. American Apparel occupies real estate in the parcel which is adjacent to the one that is the source of the dispute.	This case has been conditionally dismissed with the parties ordered to negotiate a settlement.
Mary Nelson v. American Apparel	May 2005	Sexual Harassment.	Discovery stage.
Navigators Insurance v. American Apparel	October 2005	Denial of insurance coverage; declaratory judgment action.	Case is stayed pursuant to agreement of both parties, pending final resolution of Mary Nelson v. American Apparel (*See above*)
Sylvia Hsu v. American Apparel: *See* Claim No. 648-378568 under Worker s Compensation Claim	Charge of Discrimination No. 480-2006-00418 was filed by Ms. Hsu with the EEOC in February 2006	EEOC Complaint Sexual Harassment.	EEOC still investigating
American Apparel v. Red Seven, *et al.*	March 2006	Breach of contract. American Apparel is suing these parties for past due balances owed for goods received.	First session of mediation completed. Settlement underway.
American Apparel v. Modern Amusement, Inc., *et al*.	March 2006	Breach of contract. American Apparel is suing these parties for past due balances owed for goods received.	Discovery phase.
American Apparel v. Stills Productions, *et al*.	March 2006	Breach of contract. American Apparel is suing these parties for past due balances owed for goods received.	Discovery phase.
American Apparel v. Garmentology	April 2006	Breach of contract. American Apparel is suing these parties for past due balances owed for goods received.	Case has settled. Defendants making installment payment on full amount owing.

A-66

Matter	Date Filed	Brief Description of Case	Current Status
American Apparel v. Prototype 21	N/A	Breach of contract. Collections matter American Apparel is suing for past due balances owed for goods received.	Demand letter sent; complaint will be filed in two weeks if no response.
American Apparel v. New Vision	June 2006	Breach of contract. American Apparel is suing these parties for past due balances owed for goods received.	Default Judgment Stage.
American Apparel v. Such-A-Tees	Unknown. This matter is currently being handled by a New York law firm; A retainer fee and contract is pending to retain and sub in a new attorney in NY.	Breach of contract. American Apparel is suing these parties for past due balances owed for goods received.	Discovery phase
American Apparel v. Americus Credit Group	August 2006	Fraudulent Transfer action to recover real property with is subject to a stipulated judgment in favor of American Apparel.	Early phase, with discovery to begin shortly.
Victoria Hutchin v. American Apparel	September 2006	Wage Claim Labor Commission	Settled. $86.50
Sunco Drywall Limited v. I.C.I. Construction Ltd. And 9156-4526 Quebec Inc.	October 2005	Past due balances.	Pending.

Table of Contents

SCHEDULE 2.12

LABOR MATTERS

Matter	Date Filed	Brief Description of Case	Current Status
Mary Nelson v. American Apparel	May 2005	Sexual Harassment.	Discovery stage.
Sylvia Hsu v. American Apparel: *see* Claim No. 648-378568 under Worker s Compensation Claim	Charge of Discrimination No. 480-2006-00418 was filed by Ms. Hsu with the EEOC in February 2006	EEOC Complaint Sexual Harassment.	EEOC still investigating
Victoria Hutchin v. American Apparel	September 2006	Wage Claim Labor Commission	Settled, $86.50

A-68

Table of Contents

SCHEDULE 2.14(b)

IMPERFECTIONS OF TITLE PERSONAL PROPERTY

On November 24, 2006 a financing statement was registered under the *Personal Property Security Act* of Ontario showing 2083497 Ontario Inc. as the debtor and the Toronto Dominion Bank as the Lender. The registration is for a period of 5 years, expiring on November 24, 2011 and covers the following collateral classification: inventory, equipment, accounts, other (motor vehicle included).

As of the current date, a financing statement is in the process of being registered under the *Personal Property Security Act* of British Columbia. The registration will show 4300840 Canada Inc. as the debtor and the Toronto Dominion Bank as the lender. The registration should be for a period of 5 years and should cover the following collateral classification: inventory, equipment, accounts, other (motor vehicle included).

As of the current date, a financing statement is in the process of being registered under the *Personal Property Security Act* of Nova Scotia. The registration will show 6338941 Canada Inc. as the debtor and the Toronto Dominion Bank as the lender. The registration should be for a period of 5 years and should cover the following collateral classification: inventory, equipment, accounts, other (motor vehicle included).

Table of Contents

SCHEDULE 2.18

INTELLECTUAL PROPERTY

DOMESTIC TRADEMARK REGISTRATIONS

Trademark	Registration Number	Issue Date
AMERICAN APPAREL	2,954,280	May 24, 2005
AMERICAN APPAREL	3,048,206	January 24, 2006
SUSTAINABLE EDITION	2,984,703	August 16, 2005
STANDARD AMERICAN	2,534,190	January 29, 2002
CLASSIC BABY	2,534,189	January 29, 2002
CLASSIC GIRL	2,534,188	January 29, 2002
CLASSICGIRL & DESIGN	3,026,295	December 13, 2005
NINE SQUARE Design	3,078,364	April 11, 2006
CLASSICBABY & Design	3,102,758	June 13, 2006
SUSTAINABLE EDITION & Design	3,102,765	June 13, 2006
STANDARD AMERICAN & Design	3,105,682	June 20, 2006
ALL AMERICAN APPAREL**	2,359,401	June 20, 2000
ALL AMERICAN APPAREL**	2,063,013	May 20, 1997

DOMESTIC TRADEMARK APPLICATIONS

Trademark	Application Number	Filing Date
SUSTAINABLE EDITION	76/585,766	April 8, 2004
AMERICAN APPAREL	76/624,848	December 16, 2004
AMERICAN APPAREL aa	76/624,848	December 16, 2004
AA Logo	76/624,847	December 16, 2004
SEVEN CIRCLE Design	76/636,803	April 25, 2005
PANTYTIME	78/738,044	October 21, 2005

INTERNATIONAL TRADEMARK REGISTRATIONS

Trademark	Country/Registration Number	Issue Date
CLASSIC GIRL & Design	Taiwan 1,052,601	August 1, 2003
CLASSIC BABY & Design	Taiwan 1,051,285	July 16, 2003
STANDARD AMERICAN & Design	Taiwan 1,078,209	January 1, 2004
AMERICAN APPAREL	Taiwan 1,210,674	May 16, 2006
STANDARD AMERICAN	Taiwan 1,213,017	June 1, 2006
STANDARD AMERICAN	Japan 4,607,407	September 27, 2002
CLASSIC BABY	Japan 4,513,151	October 12, 2001
CLASSIC GIRL & Design	Japan 4,513,149	October 12, 2001
Classic Baby Design	Japan 4,513,150	October 12, 2001
Classic Girl Design	Japan 4,513,148	October 12, 2001
AMERICAN APPAREL	MadridProt.-868568	June 22, 2005
AMERICAN APPAREL aa	MadridProt.-868810	September 11, 2004
AMERICAN APPAREL. NET	CTM 3094927	December 7, 2004
aa Logo	CTM 3254604	January 1, 2005
GIRLY T	CTM 2793768	October 30, 2003
CLASSIC BABY & Design	CTM 2769560	March 12, 2004
CLASSIC BABY & Design	CTM 3254638	April 12, 2005

Table of Contents

INTERNATIONAL TRADEMARK REGISTRATIONS (Continued)

Trademark	Country/Registration Number	Issue Date
STANDARD AMERICAN & Design	CTM 2769586	November 20, 2003
STANDARD AMERICAN & Design	CTM 3254554	November 15, 2004
SUSTAINABLE EDITION aa Logo	CTM 3983434	December 5, 2005
AA Logo	PR China 3232543	January 14, 2004
CLASSIC BABY & Design	PR China 3232541	January 14, 2004
americanapparel.net	PR China 1144226	March 16, 2005
CLASSIC BABY	PR China 1202269	April 1, 2006
CLASSIC GIRL	PR China 1202270	April 1, 2006
Circle Design	PR China 1202267	April 1, 2006
Square Design	PR China 1202266	April 1, 2006
SUSTAINABLE EDITION Flower Design	PR China 1202265	April 1, 2006