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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2016

OR

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

For the transition period from – to –

Commission file number: 001-35629

TILE SHOP HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation)

45-5538095
(I.R.S. Employer Identification No.)

14000 Carlson Parkway
Plymouth, Minnesota
(Address of principal executive offices)

55441
(Zip Code)

(763) 852-2988
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of April 22, 2016, there were 51,493,590 shares of the registrant's common stock, par value \$0.0001 per share, outstanding.

TILE SHOP HOLDINGS, INC.
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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS**Tile Shop Holdings, Inc. and Subsidiaries**
Consolidated Balance Sheets
(dollars in thousands, except share and per share data)
(unaudited)

	March 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 16,405	\$ 10,330
Restricted cash	219	219
Trade receivables, net	2,368	1,966
Inventories	64,236	69,878
Prepaid inventory	378	568
Income tax receivable	363	735
Other current assets, net	3,188	3,557
Total Current Assets	87,157	87,253
Property, plant and equipment, net	136,004	135,115
Deferred tax assets	20,563	20,846
Other assets	1,734	1,793
Total Assets	\$ 245,458	\$ 245,007
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 14,204	\$ 14,584
Current portion of long-term debt	4,806	4,744
Income tax payable	3,583	1,101
Other accrued liabilities	23,930	19,327
Total Current Liabilities	46,523	39,756
Long-term debt, net	36,226	51,178
Capital lease obligation, net	775	797
Deferred rent	35,812	34,983
Other long-term liabilities	2,923	3,092
Total Liabilities	122,259	129,806
Stockholders' Equity:		
Common stock, par value \$0.0001; authorized: 100,000,000 shares; issued and outstanding: 51,438,973 and 51,437,973 shares, respectively	5	5
Preferred stock, par value \$0.0001; authorized: 10,000,000 shares; issued and outstanding: 0 shares	-	-
Additional paid-in-capital	181,430	180,192
Accumulated deficit	(58,227)	(64,985)
Accumulated other comprehensive (loss) income	(9)	(11)
Total Stockholders' Equity	123,199	115,201
Total Liabilities and Stockholders' Equity	\$ 245,458	\$ 245,007

See accompanying Notes to Consolidated Financial Statements.

Tile Shop Holdings, Inc. and Subsidiaries
Consolidated Statements of Operations
(dollars in thousands, except per share data)
(unaudited)

	Three Months Ended	
	March 31,	
	2016	2015
Net sales	\$ 84,714	\$ 72,963
Cost of sales	25,009	21,992
Gross profit	59,705	50,971
Selling, general and administrative expenses	47,949	43,776
Income from operations	11,756	7,195
Interest expense	(570)	(803)
Other income	31	29
Income before income taxes	11,217	6,421
Provision for income taxes	(4,459)	(2,762)
Net income	\$ 6,758	\$ 3,659
Income per common share:		
Basic	\$ 0.13	\$ 0.07
Diluted	\$ 0.13	\$ 0.07
Weighted average shares outstanding:		
Basic	51,359,167	51,125,221
Diluted	51,666,432	51,163,963

See accompanying Notes to Consolidated Financial Statements.

Tile Shop Holdings, Inc. and Subsidiaries
Consolidated Statements of Comprehensive (Loss) Income
(dollars in thousands)
(unaudited)

	Three Months Ended	
	March 31,	
	2016	2015
Net income	\$ 6,758	\$ 3,659
Currency translation adjustment, net of provision for taxes of \$1 and \$0	2	-
Other comprehensive income	2	-
Comprehensive income	\$ 6,760	\$ 3,659

See accompanying Notes to Consolidated Financial Statements.

Tile Shop Holdings, Inc. and Subsidiaries
Consolidated Statements of Stockholders' Equity (Deficit)
(dollars in thousands, except share data)
(unaudited)

	<u>Common stock</u>							
	Shares	Amount	Additional paid-in capital	Treasury units	Retained earnings (deficit)	Accumulated other comprehensive income (loss)	Total	
Balance at December 31, 2014	51,314,005	\$ 5	\$ 174,371	\$ -	\$ (80,681)	\$ -	\$ 93,695	
Issuance of restricted shares	54,036	-	-	-	-	-	-	
Stock based compensation	-	-	5,545	-	-	-	5,545	
Stock option exercises	69,932	-	276	-	-	-	276	
Foreign currency translation adjustments	-	-	-	-	-	(11)	(11)	
Net income	-	-	-	-	15,696	-	15,696	
Balance at December 31, 2015	<u>51,437,973</u>	<u>\$ 5</u>	<u>\$ 180,192</u>	<u>\$ -</u>	<u>\$ (64,985)</u>	<u>\$ (11)</u>	<u>\$ 115,201</u>	
Stock based compensation	-	-	1,229	-	-	-	1,229	
Stock option exercises	1,000	-	9	-	-	-	9	
Foreign currency translation adjustments	-	-	-	-	-	2	2	
Net income	-	-	-	-	6,758	-	6,758	
Balance at March 31, 2016	<u>51,438,973</u>	<u>\$ 5</u>	<u>\$ 181,430</u>	<u>\$ -</u>	<u>\$ (58,227)</u>	<u>\$ (9)</u>	<u>\$ 123,199</u>	

See accompanying Notes to Consolidated Financial Statements.

Tile Shop Holdings, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(dollars in thousands)
(unaudited)

	Three Months Ended	
	March 31,	
	2016	2015
Cash Flows From Operating Activities		
Net income	\$ 6,758	\$ 3,659
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation & amortization	5,571	5,649
Amortization of debt issuance costs	157	116
Loss on disposals of property, plant and equipment	70	12
Deferred rent	678	866
Stock based compensation	1,229	1,305
Deferred income taxes	283	(1,001)
Changes in operating assets and liabilities:		
Trade receivables	(402)	(552)
Inventories	5,642	5,957
Prepaid expenses and other current assets	576	(424)
Accounts payable	(703)	(1,144)
Income tax receivable/ payable	2,852	6,931
Accrued expenses and other liabilities	4,762	4,752
Net cash provided by operating activities	<u>27,473</u>	<u>26,126</u>
Cash Flows From Investing Activities		
Purchases of property, plant and equipment	(6,375)	(4,575)
Net cash used in investing activities	<u>(6,375)</u>	<u>(4,575)</u>
Cash Flows From Financing Activities		
Payments of long-term debt and capital lease obligations	(15,031)	(23,360)
Advances on line of credit	-	5,000
Proceeds from exercise of stock options	9	10
Security deposits	(3)	(1)
Net cash used in financing activities	<u>(15,025)</u>	<u>(18,351)</u>
Effect of exchange rate changes on cash	2	-
Net change in cash	6,075	3,200
Cash and cash equivalents beginning of period	10,330	5,759
Cash and cash equivalents end of period	<u>\$ 16,405</u>	<u>\$ 8,959</u>
Supplemental disclosure of cash flow information		
Purchases of property, plant and equipment included in accounts payable and accrued expenses	\$ 1,052	\$ 467
Cash paid for interest	673	776
Cash paid (received) for income taxes, net of refunds	1,607	(4,168)

See accompanying Notes to Consolidated Financial Statements.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Note 1: Background

The Tile Shop, LLC (“The Tile Shop”) was formed on December 30, 2002, as a Delaware limited liability company and began operations on January 1, 2003. Tile Shop Holdings, Inc. (“Holdings,” and together with its wholly owned subsidiaries, the “Company”) was incorporated under the laws of the state of Delaware in June 2012 to become the parent company of The Tile Shop, LLC.

The Company is engaged in the sale of tile, stone, glass, and other flooring products. The Company also manufactures setting and maintenance materials in Michigan, Virginia, Oklahoma and Wisconsin. The Company’s primary market is retail sales to consumers, contractors, designers and home builders. As of March 31, 2016, the Company had 115 stores in 31 states and an on-line retail operation. The Company also has distribution centers located in Michigan, Virginia, Oklahoma and Wisconsin. The Company has a sourcing operation located in China.

The accompanying Consolidated Financial Statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the rules and regulations for reporting on Form 10-Q. Accordingly, they do not include certain information and disclosures required for comprehensive financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal recurring nature, including the elimination of all intercompany transactions. Operating results for the three months ended March 31, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2016.

These statements should be read in conjunction with the Consolidated Financial Statements and footnotes included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015. The accounting policies used in preparing these Consolidated Financial Statements are the same as those described in Note 1 to the Consolidated Financial Statements in such Form 10-K. Certain prior year amounts have been reclassified to conform to current year presentation.

Change in Accounting Principle

In April 2015, the Financial Accounting Standards Board (FASB) issued a standard that requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability.

The Company historically presented debt issuance costs, or fees paid to third party advisors related to directly issuing debt, as assets on the Consolidated Balance Sheet. The guidance simplifies the presentation of debt issuance costs by requiring debt issuance costs to be presented as a deduction from the corresponding liability, consistent with debt discounts. This guidance gives entities the ability to make a policy election regarding the classification of debt issuance costs associated with revolving line of credit agreements. The Company has elected to present the unamortized debt issuance costs associated with its revolving line of credit as other assets in the Consolidated Balance Sheet. Unamortized deferred financing costs attributable to the new market tax credit program are also classified as other assets in the Consolidated Balance Sheet. The Company has applied this guidance retrospectively to the prior period Consolidated Balance Sheet.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

The reclassification did not impact net income previously reported or any prior amounts reported on the Consolidated Statements of Operations. The following table presents the effect of the retrospective application of this change in accounting principle on the Company's Consolidated Balance Sheet as of December 31, 2015:

	As Reported December 31, 2015	(in thousands) Effect of Change in Accounting Principle	As Adjusted December 31, 2015
Assets			
Current assets:			
Other current assets, net	\$ 3,656	\$ (99)	\$ 3,557
Total Current Assets	87,352	(99)	87,253
Noncurrent assets:			
Other assets	2,122	(329)	1,793
Total Assets	<u>\$ 245,435</u>	<u>\$ (428)</u>	<u>\$ 245,007</u>
Liabilities and Stockholders' Equity			
Current liabilities:			
Current portion of long-term debt	\$ 5,095	\$ (351)	\$ 4,744
Long-term Liabilities:			
Long-term debt, net	51,255	(77)	51,178
Total Liabilities	130,234	(428)	129,806
Total Liabilities and Stockholders' Equity	<u>\$ 245,435</u>	<u>\$ (428)</u>	<u>\$ 245,007</u>

Note 2: Inventories

Inventories are stated at the lower of cost (determined on the weighted average cost method) or market. Inventories consist primarily of merchandise held for sale. Inventories were comprised of the following as of March 31, 2016 and December 31, 2015:

	(in thousands)	
	March 31, 2016	December 31, 2015
Finished goods	\$ 57,199	\$ 59,503
Raw materials	2,687	2,681
Finished goods in transit	4,350	7,694
Total	<u>\$ 64,236</u>	<u>\$ 69,878</u>

The Company records provisions for losses related to shrinkage and other amounts that are otherwise not expected to be fully recoverable. These provisions are calculated based on historical shrinkage, selling price, margin and current business trends.

Note 3: Income taxes

The Company's effective tax rate on net income before income taxes for the three months ended March 31, 2016 and 2015 was 39.8% and 43.0%, respectively. During the three months ended March 31, 2015, the Company recognized an increase in tax expense in connection with certain state income tax changes enacted during the quarter. State tax rate changes did not have a significant impact on the effective tax rate during the three months ended March 31, 2016. For the three months ended March 31, 2016 and 2015, the Company recorded a provision for income taxes of \$4.5 million and \$2.8 million, respectively.

The Company records interest and penalties relating to uncertain tax positions in income tax expense. As of March 31, 2016 and 2015, the Company has not recognized any liabilities for uncertain tax positions nor have interest and penalties related to uncertain tax positions been accrued.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Note 4: Earnings Per Share

Basic earnings per share is calculated by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted earnings per share is calculated by dividing net income by the weighted-average number of common shares outstanding, after taking into consideration all dilutive potential shares outstanding during the period.

Basic and diluted earnings per share were calculated as follows:

	(dollars in thousands)	
	For the three months ended	
	March 31,	
	2016	2015
Net income	\$ 6,758	\$ 3,659
Weighted average basic shares outstanding	51,359,167	51,125,221
Effect of dilutive securities attributable to stock-based awards	307,265	38,742
Weighted average diluted shares outstanding	51,666,432	51,163,963
Income per common share:		
Basic	\$ 0.13	\$ 0.07
Dilutive	\$ 0.13	\$ 0.07
Anti-dilutive securities excluded from EPS calculation	303,008	1,750,735

Note 5: Other Accrued Liabilities

Other accrued liabilities consisted of the following:

	(in thousands)	
	March 31,	December 31,
	2016	2015
Customer deposits	\$ 8,481	\$ 6,026
Accrued wages and salaries	5,120	4,336
Sales return reserve	3,156	2,781
Taxes	3,960	3,043
Other accrued liabilities	3,213	3,141
Total other accrued liabilities	\$ 23,930	\$ 19,327

Note 6: Long-term Debt

On June 2, 2015, the Company and its operating subsidiary, The Tile Shop, LLC, entered into a credit agreement with Fifth Third Bank, Bank of America, N.A., and Huntington National Bank (the "Credit Agreement"). The Credit Agreement provides the Company with a \$125.0 million senior secured credit facility, comprised of a five-year \$50.0 million term loan and a \$75.0 million revolving line of credit. The Credit Agreement is secured by virtually all of the assets of the Company, including but not limited to, inventory, receivables, equipment and real property. Borrowings pursuant to the Credit Agreement bear interest at either a base rate or a LIBOR-based rate, at the option of the Company. The LIBOR-based rate will range from LIBOR plus 1.50% to 2.00%, depending on The Tile Shop's leverage ratio. The base rate is equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Fifth Third Bank "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.50% to 1.00% depending on The Tile Shop's leverage ratio. At March 31, 2016 the base interest rate was 4.25% and the LIBOR-based interest rate was 2.19%. Borrowings outstanding consisted of \$40.5 million on the term loan as of March 31, 2016. The Company can elect to prepay the term loan without incurring a penalty. Additional borrowings pursuant to the Credit Agreement may be used to support the Company's growth and for working capital purposes. The Company incurred \$1.0 million of debt issuance costs in connection with the Credit Agreement and will be amortized over the five-year life of the Credit Agreement. Debt issuance costs attributable to the term loan are classified as a reduction of debt in the Consolidated Balance Sheet. Debt issuance costs attributable to the revolving line of credit are classified as assets in the Consolidated Balance Sheet. The term loan requires quarterly principal payments as follows (in thousands):

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Period

June 30, 2016 to June 30, 2017	\$ 1,250
September 30, 2017 to June 30, 2018	1,875
September 30, 2018 to March 31, 2020	2,500

The Credit Agreement contains customary events of default, conditions to borrowings, and restrictive covenants, including restrictions on the Company's ability to dispose of assets, make acquisitions, incur additional debt, incur liens, make investments, or enter into transactions with affiliates on other than terms that could be obtained in an arm's length transaction. The Credit Agreement also includes financial and other covenants including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios. In addition, except with respect to pro rata payments made by The Tile Shop or other subsidiaries to Holdings or any other equity owner of such entity, the Credit Agreement prohibits the payments of cash dividends. The Company was in compliance with the covenants as of March 31, 2016.

Long-term debt consists of the following at March 31, 2016 and December 31, 2015 (in thousands):

	March 31, 2016		December 31, 2015	
	Unamortized Debt Issuance		Unamortized Debt Issuance	
	Principal	Costs	Principal	Costs
Term note payable - interest at 2.19% and 2.18% at March 31, 2016 and December 31, 2015, respectively	\$ 40,450	\$ (317)	\$ 47,450	\$ (428)
Commercial bank credit facility	-	-	8,000	-
Variable interest rate bonds (0.35% at both March 31, 2016 and December 31, 2015), which mature April 1, 2023, collateralized by buildings and equipment	900	-	900	-
Total debt obligations	41,350	(317)	56,350	(428)
Less: current portion	5,095	(289)	5,095	(351)
Debt obligations, net of current portion	\$ 36,255	\$ (28)	\$ 51,255	\$ (77)

Note 7: Fair Value of Financial Instruments

These consolidated financial statements include the following financial instruments: cash and cash equivalents, trade receivables, accounts payable, accrued expenses, capital leases, notes payable, and debt. At March 31, 2016 and December 31, 2015, the carrying amount of the Company's cash and cash equivalents, trade receivables, accounts payable and accrued expenses approximated their fair values due to their short-term maturities. The carrying value of the Company's borrowings and capital lease obligation approximates fair value based upon the market interest rates available to the Company for debt and capital lease obligations with similar risk and maturities.

Fair value is the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. To measure fair value, the Company uses a three-tier valuation hierarchy based upon observable and non-observable inputs:

Level 1 – Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 – Significant other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

Level 3 – Significant unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management’s estimates of market participant assumptions.

Note 8: Equity Incentive Plans

Stock options:

The Company measures and recognizes compensation expense for all stock-based awards at fair value. The financial statements for the three months ended March 31, 2016 and 2015 include compensation cost for the portion of outstanding awards that vested during those periods. The Company recognizes stock-based compensation costs on a straight-line basis over the requisite service period of the award, which is generally the option vesting term. Total stock-based compensation expense related to stock options was \$1.0 million and \$0.8 million for the three months ended March 31, 2016 and 2015, respectively. Stock-based compensation expense is included in selling, general and administrative expenses in the accompanying Consolidated Statements of Operations.

As of March 31, 2016, the Company had outstanding stock options to purchase 2,800,945 shares of common stock at a weighted average exercise price of \$13.06.

Restricted stock:

The Company awards restricted common shares to selected employees, and non-employee directors. Recipients are not required to provide any consideration other than continued service. Restricted share awards are subject to certain restrictions on transfer, and all or part of the shares awarded may be subject to forfeiture upon the occurrence of certain events, including employment termination. The restricted stock is valued at its grant date fair value and expensed over the requisite service period or the vesting term of the awards. Total stock-based compensation expense related to restricted stock was \$0.2 million and \$0.5 million for the three months ended March 31, 2016 and 2015, respectively. Stock-based compensation expense is included in selling, general and administrative expenses in the accompanying Consolidated Statements of Operations.

As of March 31, 2016, the Company had 79,036 outstanding restricted common shares.

Note 9: New Market Tax Credit

In July 2013 the Company entered into a financing transaction with Chase Community Equity (“Chase”), and U.S. Bank Community, LLC (“U.S. Bank”, and, collectively with Chase, the “investors”) related to a \$19.1 million acquisition, rehabilitation and construction of the Company’s new distribution and manufacturing center in Durant, Oklahoma. The investors made a capital contribution to, and Tile Shop Lending made a loan to Chase New Market Tax Credit, The Tile Shop of Oklahoma Investment Fund, LLC, and The Tile Shop Investment Fund LLC (the “Investment Funds”) under a qualified New Markets Tax Credit (“NMTC”) program. The NMTC program was provided for in the Community Renewal Tax Relief Act of 2000 (the “Act”) and is intended to induce capital investment in qualified lower income communities. The Act permits taxpayers to claim credits against their Federal income taxes for up to 39% of qualified investments in the equity of community development entities (“CDEs”). CDEs are privately managed investment institutions that are certified to make qualified low-income community investments.

In July 2013, Tile Shop Lending loaned \$13.5 million to the Investment Funds at an interest rate of 1.35% per year and with a maturity of September 30, 2043. The Investment Funds then contributed the loan to certain CDEs, which, in turn, loaned the funds on similar terms to Tile Shop of Oklahoma, LLC, an indirect, wholly-owned subsidiary of the Company. The proceeds of the loans from the CDEs (including loans representing the capital contribution made by the investors, net of syndication fees) were used to partially fund the new manufacturing and distribution center project.

In July 2013, the investors also contributed \$5.6 million to the Investment Funds and, by virtue of such contribution, are entitled to substantially all of the tax benefits derived from the NMTCs, while the Company effectively received net loan proceeds equal to the investors’ contributions to the Investment Fund. This transaction includes a put/call provision whereby the Company may be obligated or entitled to repurchase the investors’ interest. The Company believes that the investors will exercise the put option in September 2020 at the end of the recapture period. The value attributed to the put/call is de minimis. The NMTC is subject to 100% recapture for a period of seven years as provided in the Internal Revenue Code. The Company is required to be in compliance with various regulations and contractual provisions that apply to the NMTC arrangement. Non-compliance with applicable requirements could result in projected tax benefits not being realized and, therefore, could require the Company to indemnify the investors for any loss or recapture of NMTCs related to the financing until such time as the obligation to deliver tax benefits is relieved. The Company does not anticipate any credit recaptures will be required in connection with this arrangement.

Tile Shop Holdings, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

The Company has determined that the financing arrangement with the Investment Funds and CDEs contains a variable interest entity (“VIE”). The ongoing activities of the Investment Funds – collecting and remitting interest and fees and NMTC compliance – were all considered in the initial design and are not expected to significantly affect economic performance throughout the life of the Investment Funds. Management considered the contractual arrangements that obligate the Company to deliver tax benefits and provide various other guarantees to the structure; Chase’s and U.S. Bank’s lack of a material interest in the underlying economics of the project; and the fact that the Company is obligated to absorb losses of the Investment Fund. The Company concluded that they are the primary beneficiary of the VIE and consolidated the Investment Funds, as a VIE, in accordance with the accounting standards for consolidation. Chase’s and U.S. Bank’s contributions of \$4.4 million, net of syndication fees, are included in cash and other long-term liabilities in the accompanying Consolidated Balance Sheet. The benefit of this net \$4.4 million contribution is recognized as a decrease in depreciation expense as the Company amortizes the contribution liability over the seven-year compliance period as it is being earned through the on-going compliance with the conditions of the NMTC program. As of March 31, 2016, the balance of the contribution liability was \$2.9 million and is classified as other long-term liabilities on the Consolidated Balance Sheet.

Note 10: Commitments and Contingencies

The Company, two of its former executive officers, five of its outside directors, and certain companies affiliated with the directors, are defendants in a consolidated class action brought under the federal securities laws and now pending in the United States District Court for the District of Minnesota under the caption Beaver County Employees’ Retirement Fund, et al. v. Tile Shop Holdings, Inc., et al. Several related actions were filed in 2013, and then consolidated. The plaintiffs are three investors who seek to represent a class or classes consisting of (1) all purchasers of Tile Shop common stock between August 22, 2012 and January 28, 2014 (the “alleged class period”), seeking to pursue remedies under the Securities Exchange Act of 1934; and (2) all purchasers of Tile Shop common stock pursuant and/or traceable to the Company’s December 2012 registration statements, seeking to pursue remedies under the Securities Act of 1933. Six firms who were underwriters in the December 2012 secondary public offering are also named as defendants. In their consolidated amended complaint (the “complaint”), the plaintiffs allege that during the alleged class period, certain defendants made false or misleading statements of material fact in press releases and SEC filings about the Company’s relationships with its vendors, its gross margins, and its supply chain and producer relationships, and that defendants failed to disclose certain related party transactions. The complaint asserts claims under Sections 11, 12(a)(2), and 15 of the Securities Act of 1933, and under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. In addition to attorney’s fees and costs, the plaintiffs seek to recover damages on behalf of the members of the purported classes. The defendants are vigorously defending the matter. The matter is now in discovery.

The Company also is a Defendant in a consolidated action brought derivatively on behalf of the Company by two shareholders of the Company. One action was first filed in the United States District Court for the District of Minnesota, and then voluntarily dismissed and re-filed in the Court of Chancery for the State of Delaware (“Delaware Chancery Court”). The second action was filed in Delaware Chancery Court. The two actions have since been consolidated by the Delaware Chancery Court under the caption In re Tile Shop Holdings, Inc. Stockholder Derivative Litigation. On July 31, 2015, the plaintiff-shareholders filed their Verified Consolidated Stockholder Derivative Complaint (“complaint”). The complaint names as defendants six members of the Company’s Board of Directors, and a former employee of the Company. The complaint tracks many of the same factual allegations as have been made in the above-described federal securities class action. It alleges that the defendant-directors breached their fiduciary duties by failing to adopt adequate internal controls for the Company, by approving false and misleading statements issued by the Company, by causing the Company to violate generally accepted accounting principles and SEC regulations, by engaging in or approving alleged insider trading, and by permitting the Company’s primary product to contain illegal amounts of lead. The complaint also alleges claims for insider trading and unjust enrichment. The complaint seeks damages, disgorgement, an award of attorneys’ fees and other expenses, and an order compelling changes to the Company’s corporate governance and internal procedures. On November 2, 2015, defendants filed a motion to dismiss the derivative action, or in the alternative, to stay it pending resolution of the Beaver County Employees’ Retirement Fund action described above. Subsequently, the parties entered into a stipulation, and the Court entered an Order, staying the derivative action until resolution of the Beaver County Employees’ Retirement Fund action described above, or until a mutually agreeable resolution of the derivative action.

Given the uncertainty of litigation and the preliminary stage of these cases, the Company cannot reasonably estimate the possible loss or range of loss that may result from these actions. The Company maintains directors and officers liability insurance policies that may reduce the Company’s exposure, if any. In the event the Company incurs a loss, the Company will pursue recoveries to the maximum extent available under these policies.

The Company is also, from time to time, subject to claims and disputes arising in the normal course of business. In the opinion of management, while the outcome of such claims and disputes cannot be predicted with certainty, the Company’s ultimate liability in connection with these matters is not expected to have a material adverse effect on the results of operations, financial position, or cash flows.

Note 11: New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued a final standard on revenue from contracts with customers. The new standard sets forth a single comprehensive model for recognizing and reporting revenue. The new standard is effective for the Company in fiscal year 2018, and permits the use of either a retrospective or a cumulative effect transition method. The Company is currently assessing the impact of implementing the new guidance on its consolidated financial statements.

In August 2014, the FASB issued a standard requiring an entity's management to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern within one year after the date of the financial statements. The guidance also sets forth a series of disclosures that are required in the event the entity's management concludes that there is substantial doubt about the entity's ability to continue as a going concern. The new standard becomes effective for the Company in fiscal 2016 and requires an ongoing evaluation at each interim and annual period thereafter. The Company is currently assessing the effect the new standard will have on its consolidated financial statements.

In April 2015, the FASB issued a standard that requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The Company adopted the provisions of this statement in the first quarter of 2016 and prior periods have been retrospectively adjusted (see "Note 1 to the Consolidated Financial Statements").

In February 2015, the FASB issued a new accounting standard that will modify current consolidation guidance. The standard makes changes to both the variable interest entity model and the voting interest entity model, including modifying the evaluation of whether limited partnerships or similar legal entities are VIEs or voting interest entities and amending the guidance for assessing how relationships of related parties affect the consolidation analysis of VIEs. The standard is effective for the Company in fiscal 2016. The adoption of this new standard did not have a material effect on the Company's financial statements.

In July 2015, the FASB issued a standard which simplifies the subsequent measurement of inventory. Currently, an entity is required to measure inventory at the lower of cost or market, whereby market can be replacement cost, net realizable value, or net realizable value less an approximately normal profit margin. The changes require that inventory be measured at the lower of cost and net realizable value, thereby eliminating the use of the other two market methodologies. Net realizable value is defined as the estimated selling prices in the ordinary course of business less reasonably predictable costs of completion, disposal, and transportation. Currently, the Company applies the net realizable value market option to measure inventories at the lower of cost or market. These changes become effective for the Company in fiscal 2017. The Company is currently assessing the effect the new standard will have on its consolidated financial statements.

In February 2016, the FASB issued a standard that primarily requires organizations that lease assets to recognize the rights and obligations created by those leases on the balance sheet. The standard is effective in 2019, with early adoption permitted. The Company is currently assessing the effect the new standard will have on its consolidated financial statements.

In March 2016, the FASB issued a standard that changes the accounting for certain aspects of share-based payments to employees. The guidance requires the recognition of the income tax effects of awards in the income statement when the awards vest or are settled, thus eliminating additional paid-in capital tax pools. The guidance also allows for the employer to repurchase more of an employee's shares for tax withholding purposes without triggering liability accounting. In addition, the guidance allows for a policy election to account for forfeitures as they occur rather than on an estimated basis. The guidance is effective in 2017 with early adoption permitted. The Company is currently assessing the effect the new standard will have on its consolidated financial statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2015 and our consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or Exchange Act. Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "intend," "may," "might," "plan," "project," "seek," "should," "target," "will," "will likely result," "would," and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, unexpected delays or expenses related to opening new stores and maintaining or renovating existing stores, changes to economic conditions and customer preferences, disruptions in our supply chain, or inventory management, competitive factors, increases to interest rates or other impacts on our ability to obtain or maintain financing, unanticipated expenses related to operating as a public company including but not limited to litigation-related expenses, and those factors disclosed in the section captioned "Risk Factors" in our Annual Report for the fiscal year ended December 31, 2015, filed with the Securities and Exchange Commission. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview and Recent Trends

We are a specialty retailer of manufactured and natural stone tiles, setting and maintenance materials, and related accessories in the United States. We offer a wide selection of products, attractive prices, and exceptional customer service in an extensive showroom setting. As of March 31, 2016, we operated 115 stores in 31 states, with an average size of 21,700 square feet. We also sell our products on our website.

We purchase our tile products and accessories directly from suppliers and manufacture our own setting and maintenance materials, such as thinsset, grout, and sealers. We believe that our long-term supplier relationships, together with our design, manufacturing and distribution capabilities, enable us to offer a broad assortment of high-quality products to our customers, who are primarily homeowners and professionals, at competitive prices. We have invested significant resources to develop our proprietary brands and product sources, and believe that we are a leading retailer of manufactured and natural stone tiles, accessories, and related materials in the United States.

We believe that the highly-fragmented United States retail tile market provides us with a significant opportunity to expand our store base. We opened 1 new store in the first three months of 2016, and opened 7 new stores in the United States during 2015. We plan to open an additional 8 to 11 stores in 2016. We believe that there will continue to be additional expansion opportunities in the United States and Canada. We expect store base growth will drive productivity and operational efficiencies. Our growth plans also require us to maintain significant inventory on-hand in order to fulfill transactions at these new locations.

For the three months ended March 31, 2016 and 2015, we reported net sales of \$84.7 million and \$73.0 million, respectively, and income from operations of \$11.8 million and \$7.2 million, respectively. The increase in sales and income from operations was primarily due to same store sales growth of 13.2% and 4.5% for the three months ended March 31, 2016 and 2015, respectively.

Net cash provided by operating activities was \$27.5 million and \$26.1 million for the three months ended March 31, 2016 and 2015, respectively, which was used to fund operations, new store construction activities, and debt repayments. We expect to continue to fund our capital expenditures and daily operations from our operating cash flows. As of March 31, 2016, we had cash of \$16.4 million and working capital of \$40.6 million.

Key Components of our Consolidated Statements of Operations

Net Sales Net sales represents total charges to customers, net of returns, and includes freight charged to customers. We recognize sales at the time that the customer takes possession of the merchandise or final delivery of the product has occurred. We recognize service revenue, which consists primarily of freight charges for home delivery, when the service has been rendered. We are required to charge and collect sales and other taxes on sales to our customers and remit these taxes back to government authorities. Total revenues do not include sales tax because we are a pass-through conduit for collecting and remitting sales tax.

Comparable store sales for the three months ended March 31, 2016 increased \$9.6 million, compared to the three months ended March 31, 2015. The table below sets forth information about our same store sales growth for the three months ended March 31, 2016 and 2015.

	For the three months ended March 31,	
	2016	2015
Same store sales growth	13.2 %	4.5 %

Our increase in same store sales growth is primarily attributable to an increase in the volume of transactions, as well as increases in average transaction size. Same store sale amounts include total charges to customers less any actual returns, and the change in the returns provision related to comparable stores. In general, we consider a store comparable on the first day of the 13th full month of operation.

Between April 1, 2015 and March 31, 2016, we opened 6 new store locations. Incremental net sales of \$2.1 million occurred in the three months ended March 31, 2016 from stores not included in the comparable store base.

Cost of Sales Cost of sales consists primarily of material costs, freight, duties, and storage and delivery of product to the customers, as well as costs associated with manufacturing of setting and maintenance materials. For the three months ended March 31, 2016 and 2015, our cost of sales as a percentage of net sales was 29.5% and 30.1%, respectively. The decrease was primarily attributable to improved collection of customer delivery revenue and inventory control process improvements.

Selling, General, and Administrative Expenses For the three months ended March 31, 2016 and 2015, our selling, general, and administrative expenses as a percentage of net sales were 56.6% and 60.0%, respectively. The decrease was primarily attributable to an increase in same store sales, which outpaced the growth of selling, general, and administrative expenses for the three months ended March 31, 2016.

Provision for Income Taxes We are subject to income tax in the United States as well as other tax jurisdictions in which we conduct business. Our effective tax rate for the three months ended March 31, 2016 and 2015 was 39.8% and 43.0%, respectively. During the three months ended March 31, 2015, we recognized an increase in tax expense in connection with certain state income tax changes enacted during the quarter. State tax rate changes did not have a significant impact on the effective tax rate during the three months ended March 31, 2016.

Non-GAAP Measures

We calculate Adjusted EBITDA by taking net income calculated in accordance with accounting principles generally accepted in the United States, or GAAP, and adjusting for interest expense, income taxes, depreciation and amortization, stock based compensation expense, and special charges consisting of litigation costs. Adjusted EBITDA margin is equal to Adjusted EBITDA divided by net sales. Free cash flows is calculated by taking net cash provided by operating activities and subtracting net cash used for capital expenditures. Non-GAAP net income excludes the special charges including investigation and litigation costs and is net of tax.

We believe that these non-GAAP measures of financial results provide useful information to management and investors regarding certain financial and business trends relating to our financial condition and results of operations. Our management uses these non-GAAP measures to compare our performance to that of prior periods for trend analyses, for purposes of determining management incentive compensation, and for budgeting and planning purposes. These measures are used in monthly financial reports prepared for management and our board of directors. We believe that the use of these non-GAAP financial measures provides an additional tool for investors to use in evaluating ongoing operating results and trends and in comparing our financial measures with other specialty retailers, many of which present similar non-GAAP financial measures to investors.

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The reconciliation of Adjusted EBITDA to net income for the three months ended March 31, 2016 and 2015 is as follows:

	(in thousands)	
	Three Months Ended	
	March 31,	
	2016	2015
Net income	\$ 6,758	\$ 3,659
Interest expense	570	803
Income taxes	4,459	2,762
Depreciation & amortization	5,571	5,649
Special charges	697	514
Stock-based compensation	1,229	1,305
Adjusted EBITDA	<u>\$ 19,284</u>	<u>\$ 14,692</u>

The reconciliation of free cash flows to net cash provided by operating activities for the three months ended March 31, 2016 and 2015 is as follows:

	(in thousands)	
	Three Months Ended	
	March 31,	
	2016	2015
Net cash provided by operating activities	\$ 27,473	\$ 26,126
Purchase of property, plant and equipment	(6,375)	(4,575)
Free cash flows	<u>\$ 21,098</u>	<u>\$ 21,551</u>

The reconciliation of Non-GAAP net income to GAAP net income for the three months ended March 31, 2016 and 2015 is as follows:

	Three Months Ended			Three Months Ended		
	March 31, 2016			March 31, 2015		
(in thousands, except share and per share data)	Pretax	Net of Tax	Per Share Amounts	Pretax	Net of Tax	Per Share Amounts
GAAP net income	\$ 11,217	\$ 6,758	\$ 0.13	\$ 6,421	\$ 3,659	\$ 0.07
Special charges:						
Litigation costs	697	420	0.01	514	292	0.01
Non-GAAP net income	<u>\$ 11,914</u>	<u>\$ 7,178</u>	<u>\$ 0.14</u>	<u>\$ 6,935</u>	<u>\$ 3,951</u>	<u>\$ 0.08</u>

Our management does not consider these non-GAAP measures in isolation or as an alternative to financial measures determined in accordance with GAAP. The principal limitations of these non-GAAP financial measures are that they exclude significant expenses and income that are required by GAAP to be recognized in our consolidated financial statements. In addition, they are subject to inherent limitations as they reflect the exercise of judgments by management about which expenses and income are excluded or included in determining these non-GAAP financial measures. In order to compensate for these limitations, management presents non-GAAP financial measures in connection with GAAP results. We urge investors to review the reconciliation of our non-GAAP financial measures to the comparable GAAP financial measures and not to rely on any single financial measure to evaluate our business.

Results of Operations**Comparison of the three months ended March 31, 2016 to the three months ended March 31, 2015**

	(in thousands)			
	2016	% of sales ⁽¹⁾	2015	% of sales
Net sales	\$ 84,714		\$ 72,963	
Cost of sales	25,009	29.5 %	21,992	30.1 %
Gross profit	59,705	70.5 %	50,971	69.9 %
Selling, general and administrative expenses	47,949	56.6 %	43,776	60.0 %
Income from operations	11,756	13.9 %	7,195	9.9 %
Interest expense	(570)	(0.7)%	(803)	(1.1)%
Other income	31	0.0 %	29	0.0 %
Income before income taxes	11,217	13.2 %	6,421	8.8 %
Provision for income taxes	(4,459)	(5.3)%	(2,762)	(3.8)%
Net income	\$ 6,758	8.0 %	\$ 3,659	5.0 %

⁽¹⁾ Amounts may not foot due to rounding.

Net Sales Net sales for the first quarter of 2016 increased \$11.7 million, or 16.1%, over the first quarter of 2015. Comparable store sales increased \$9.6 million during the first quarter of 2016 due to an increase in the volume of transactions, as well as an increase in the average transaction size. Net sales for the 6 new stores open less than twelve months were \$2.1 million during the first quarter of 2016.

Gross profit Gross profit for the first quarter of 2016 increased \$8.7 million, or 17.1%, compared to the first quarter of 2015, primarily due to the increase in net sales. The gross margin rate increased from 69.9% for the first quarter of 2015 to 70.5% for the first quarter of 2016. The increase in the gross margin rate was primarily attributable to improved collection of customer delivery revenue and inventory control process improvements.

Selling, General, and Administrative Expenses Selling, general, and administrative expenses for the first quarter of 2016 increased \$4.2 million, or 9.5%, compared to the first quarter of 2015. The increase in selling, general, and administrative expenses was primarily due to an increase in compensation and benefit costs of \$3.3 million and occupancy costs of \$0.6 million as a result of opening 6 new stores during the period from April 1, 2015 through March 31, 2016, and an increase in variable compensation associated with a 13.2% increase in comparable store sales for the three months ended March 31, 2016. Selling, general, and administrative expenses as a percentage of net sales decreased to 56.6% for the first quarter of 2016 compared to 60.0% for the first quarter of 2015. The decrease in selling, general, and administrative expenses as a percentage of net sales was primarily due to a maturing store base that has higher net sales levels, which outpaced the growth of selling, general, and administrative expenses.

Selling, general, and administrative expenses include costs of \$0.7 million and \$0.5 million for each of the first quarters of 2016 and 2015, respectively, which relate to special charges consisting of litigation expenses.

Pre-opening Costs Our pre-opening costs are those typically associated with the opening of a new store and generally include rent expense, payroll costs and promotional costs. We expense pre-opening costs as incurred and include these costs in selling, general and administrative expenses. During the first quarter of 2016 and 2015, we incurred pre-opening costs of \$0.2 million and \$0.1 million, respectively.

Interest Expense Interest expense decreased \$0.2 million for the first quarter of 2016 compared to the first quarter of 2015. The decrease is primarily due to the decrease in the debt balance in 2016.

Provision for Income Taxes Income tax provision increased \$1.7 million for the first quarter of 2016 compared to the first quarter of 2015 due to higher income before income taxes in the first quarter of 2016. Our effective tax rate for the three months ended March 31, 2016 and 2015 was 39.8% and 43.0%, respectively. During the three months ended March 31, 2015, we recognized an increase in tax expense in connection with certain state income tax changes enacted during the quarter. State tax rate changes did not have a significant impact on the effective tax rate during the three months ended March 31, 2016.

Liquidity and Capital Resources

Our principal uses of liquidity have been investments in working capital and capital expenditures. Our principal sources of liquidity are \$16.4 million of cash and cash equivalents at March 31, 2016, our cash flow from operations, and borrowings available under our credit facility. We expect to use this liquidity for opening new stores, purchasing additional merchandise inventory, maintaining our existing stores, reducing outstanding debt, and general corporate purposes.

On June 2, 2015, we and our operating subsidiary, The Tile Shop, LLC, entered into a credit agreement with Fifth Third Bank, Bank of America, N.A., and Huntington National Bank (the "Credit Agreement"). The Credit Agreement provides us with a \$125.0 million senior secured credit facility, comprised of a five-year \$50.0 million term loan and a \$75.0 million revolving line of credit. The Credit Agreement is secured by virtually all of our assets, including but not limited to, inventory, receivables, equipment and real property. Borrowings pursuant to the Credit Agreement bear interest at either a base rate or a LIBOR-based rate, at our option. The LIBOR-based rate will range from LIBOR plus 1.50% to 2.00%, depending on The Tile Shop's leverage ratio. The base rate is equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Fifth Third Bank "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.50% to 1.00% depending on The Tile Shop's leverage ratio. At March 31, 2016 the base interest rate was 4.25% and the LIBOR-based interest rate was 2.19%. Borrowings outstanding consisted of \$40.5 million on the term loan as of March 31, 2016. We can elect to prepay the term loan without incurring a penalty. The term loan requires quarterly principal payments as follows (in thousands):

Period

June 30, 2016 to June 30, 2017	\$	1,250
September 30, 2017 to June 30, 2018		1,875
September 30, 2018 to March 31, 2020		2,500

The Credit Agreement contains customary events of default, conditions to borrowings, and restrictive covenants, including restrictions on our ability to dispose of assets, make acquisitions, incur additional debt, incur liens, make investments, or enter into transactions with affiliates on other than terms that could be obtained in an arm's length transaction. The Credit Agreement also includes financial and other covenants including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios. In addition, except with respect to pro rata payments made by The Tile Shop or other subsidiaries to Holdings or any other equity owner of such entity, the Credit Agreement prohibits the payments of cash dividends. We were in compliance with the covenants as of March 31, 2016.

We believe that our cash flow from operations, together with our existing cash and cash equivalents, and borrowings available under our credit facility will be sufficient to fund our operations and anticipated capital expenditures over at least the next 12 months.

Capital expenditures paid in the three months ended March 31, 2016 were \$6.4 million. Approximately \$4.2 million of this was for new store build-out, remodels of existing stores, and merchandising projects. The remainder was for general corporate and information technology purposes.

Our future capital requirements will vary based on the number of additional stores, distribution centers, and manufacturing facilities that we open and the number of stores that we choose to renovate. Our decisions regarding opening, relocating, or renovating stores, and whether to engage in strategic acquisitions, will be based in part on macroeconomic factors and the general state of the U.S. economy, as well as the local economies in the markets in which our stores are located. We intend to open an additional 8 to 11 stores during 2016. Total capital expenditures are expected to be between \$25 million and \$30 million in 2016.

Cash flows

The following table summarizes our cash flow data for the three months ended March 31, 2016 and 2015.

	(in thousands)	
	Three Months Ended	
	March 31,	
	2016	2015
Net cash provided by operating activities	\$ 27,473	\$ 26,126
Net cash used in investing activities	(6,375)	(4,575)
Net cash used in financing activities	(15,025)	(18,351)

Operating activities

Cash provided by operating activities during the three months ended March 31, 2016 was \$27.5 million, compared to \$26.1 million during the three months ended March 31, 2015. The increase is attributable to an increase in net income.

Investing activities

Net cash used in investing activities totaled \$6.4 million for the three months ended March 31, 2016, compared to \$4.6 million for the three months ended March 31, 2015. Net cash used in investing activities in each period was primarily for capital purchases of store fixtures, equipment, building improvements and leasehold improvements for stores opened or remodeled, asset additions in our distribution and manufacturing facilities, and general corporate information technology assets.

Financing activities

Net cash used in financing activities was \$15.0 million for the three months ended March 31, 2016, compared to \$18.4 million for the three months ended March 31, 2015. Cash used in financing activities during the three months ended March 31, 2016 was primarily for payments of long-term debt and capital lease obligations of \$15.0 million. At March 31, 2016, we were in compliance with our debt covenants. We intend to make principal payments due in future periods using cash from operations.

Cash and cash equivalents totaled \$16.4 million at March 31, 2016, versus \$10.3 million at December 31, 2015. We have working capital of \$40.6 million at March 31, 2016, compared to working capital of \$47.5 million at December 31, 2015.

Off-balance sheet arrangements

As of March 31, 2016 and December 31, 2015, we did not have any “off-balance sheet arrangements” (as such term is defined in Item 303 of Regulation S-K) that could have a current or future effect on our financial condition, changes in financial condition, net sales or expenses, results of operations, liquidity, capital expenditures or capital resources.

Contractual arrangements

As of March 31, 2016, there were no material changes to our contractual obligations outside the ordinary course of business.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued a final standard on revenue from contracts with customers. The new standard sets forth a single comprehensive model for recognizing and reporting revenue. The new standard is effective in fiscal year 2018, and permits the use of either a retrospective or a cumulative effect transition method. We are currently assessing the impact of implementing the new guidance on our consolidated financial statements.

In August 2014, the FASB issued a standard requiring an entity’s management to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern within one year after the date of the financial statements. The guidance also sets forth a series of disclosures that are required in the event the entity’s management concludes that there is substantial doubt about the entity’s ability to continue as a going concern. The new standard becomes effective in fiscal 2016 and requires an ongoing evaluation at each interim and annual period thereafter. We are currently assessing the effect the new standard will have on our consolidated financial statements.

In April 2015, the FASB issued a standard that requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. We adopted the provisions of this statement in the first quarter of 2016 and prior periods have been retrospectively adjusted (see “Note 1 to the Consolidated Financial Statements”).

In February 2015, the FASB issued a new accounting standard that will modify current consolidation guidance. The standard makes changes to both the variable interest entity model and the voting interest entity model, including modifying the evaluation of whether limited partnerships or similar legal entities are VIEs or voting interest entities and amending the guidance for assessing how relationships of related parties affect the consolidation analysis of VIEs. The standard is effective in fiscal 2016. The adoption of this new standard did not have a material effect on our financial statements.

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In July 2015, the FASB issued a standard which simplifies the subsequent measurement of inventory. Currently, an entity is required to measure inventory at the lower of cost or market, whereby market can be replacement cost, net realizable value, or net realizable value less an approximately normal profit margin. The changes require that inventory be measured at the lower of cost and net realizable value, thereby eliminating the use of the other two market methodologies. Net realizable value is defined as the estimated selling prices in the ordinary course of business less reasonably predictable costs of completion, disposal, and transportation. Currently, we apply the net realizable value market option to measure inventories at the lower of cost or market. These changes become effective in fiscal 2017. We are currently assessing the effect the new standard will have on our consolidated financial statements.

In February 2016, the FASB issued a standard that primarily requires organizations that lease assets to recognize the rights and obligations created by those leases on the balance sheet. The standard is effective in 2019, with early adoption permitted. We are currently assessing the effect the new standard will have on our consolidated financial statements.

In March 2016, the FASB issued a standard that changes the accounting for certain aspects of share-based payments to employees. The guidance requires the recognition of the income tax effects of awards in the income statement when the awards vest or are settled, thus eliminating additional paid-in capital tax pools. The guidance also allows for the employer to repurchase more of an employee's shares for tax withholding purposes without triggering liability accounting. In addition, the guidance allows for a policy election to account for forfeitures as they occur rather than on an estimated basis. The guidance is effective in 2017 with early adoption permitted. We are currently assessing the effect the new standard will have on our consolidated financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in our primary risk exposures or management of market risks from those disclosed in our Form 10-K for the fiscal year ended December 31, 2015.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We have established disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that information relating to the Company is accumulated and communicated to management, including our principal officers as appropriate to allow timely decisions regarding required disclosure. Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2016 and have concluded that such disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

Changes in Internal Control over Financial Reporting

No changes to our internal control over financial reporting occurring during the quarter ended March 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act).

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company, two of its former executive officers, five of its outside directors, and certain companies affiliated with the directors, are defendants in a consolidated class action brought under the federal securities laws and now pending in the United States District Court for the District of Minnesota under the caption Beaver County Employees' Retirement Fund, et al. v. Tile Shop Holdings, Inc., et al. Several related actions were filed in 2013, and then consolidated. The plaintiffs are three investors who seek to represent a class or classes consisting of (1) all purchasers of Tile Shop common stock between August 22, 2012 and January 28, 2014 (the "alleged class period"), seeking to pursue remedies under the Securities Exchange Act of 1934; and (2) all purchasers of Tile Shop common stock pursuant and/or traceable to the Company's December 2012 registration statements, seeking to pursue remedies under the Securities Act of 1933. Six firms who were underwriters in the December 2012 secondary public offering are also named as defendants. In their consolidated amended complaint (the "complaint"), the plaintiffs allege that during the alleged class period, certain defendants made false or misleading statements of material fact in press releases and SEC filings about the Company's relationships with its vendors, its gross margins, and its supply chain and producer relationships, and that defendants failed to disclose certain related party transactions. The complaint asserts claims under Sections 11, 12(a)(2), and 15 of the Securities Act of 1933, and under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. In addition to attorney's fees and costs, the plaintiffs seek to recover damages on behalf of the members of the purported classes. The defendants are vigorously defending the matter. The matter is now in discovery.

The Company also is a Defendant in a consolidated action brought derivatively on behalf of the Company by two shareholders of the Company. One action was first filed in the United States District Court for the District of Minnesota, and then voluntarily dismissed and re-filed in the Court of Chancery for the State of Delaware ("Delaware Chancery Court"). The second action was filed in Delaware Chancery Court. The two actions have since been consolidated by the Delaware Chancery Court under the caption In re Tile Shop Holdings, Inc. Stockholder Derivative Litigation. On July 31, 2015, the plaintiff-shareholders filed their Verified Consolidated Stockholder Derivative Complaint ("complaint"). The complaint names as defendants six members of the Company's Board of Directors, and a former employee of the Company. The complaint tracks many of the same factual allegations as have been made in the above-described federal securities class action. It alleges that the defendant-directors breached their fiduciary duties by failing to adopt adequate internal controls for the Company, by approving false and misleading statements issued by the Company, by causing the Company to violate generally accepted accounting principles and SEC regulations, by engaging in or approving alleged insider trading, and by permitting the Company's primary product to contain illegal amounts of lead. The complaint also alleges claims for insider trading and unjust enrichment. The complaint seeks damages, disgorgement, an award of attorneys' fees and other expenses, and an order compelling changes to the Company's corporate governance and internal procedures. On November 2, 2015, defendants filed a motion to dismiss the derivative action, or in the alternative, to stay it pending resolution of the Beaver County Employees' Retirement Fund action described above. Subsequently, the parties entered into a stipulation, and the Court entered an Order, staying the derivative action until resolution of the Beaver County Employees' Retirement Fund action described above, or until a mutually agreeable resolution of the derivative action.

Given the uncertainty of litigation and the preliminary stage of these cases, the Company cannot reasonably estimate the possible loss or range of loss that may result from these actions. The Company maintains directors and officers liability insurance policies that may reduce the Company's exposure, if any. In the event the Company incurs a loss, the Company will pursue recoveries to the maximum extent available under these policies.

The Company is also, from time to time, subject to claims and disputes arising in the normal course of business. In the opinion of management, while the outcome of such claims and disputes cannot be predicted with certainty, the Company's ultimate liability in connection with these matters is not expected to have a material adverse effect on the results of operations, financial position, or cash flows.

ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibits

3.1	Certificate of Incorporation of Tile Shop Holdings, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Registration Statement on Form S-4 filed with the Securities and Exchange Commission on July 2, 2012).
3.2	By-Laws of Tile Shop Holdings, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form S-4 filed with the Securities and Exchange Commission on July 2, 2012).
10.1*	Offer Letter Agreement, between Tile Shop Holdings, Inc. and Lynda Stout, dated February 29, 2016.
21.1*	Subsidiaries of Tile Shop Holdings, Inc.
31.1*	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
32.1**	Certifications of Chief Executive Officer Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
32.2**	Certifications of Chief Financial Officer Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

* Filed herewith

** Furnished herewith

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TILE SHOP HOLDINGS, INC.

Dated: April 28, 2016

By: /s/ CHRIS R. HOMEISTER
Chris R. Homeister
Chief Executive Officer

Dated: April 28, 2016

By: /s/ KIRK L. GEADELMANN
Kirk L. Geadelmann
Chief Financial Officer

**TILE SHOP HOLDINGS, INC.
EXHIBIT INDEX**

Exhibit

No.	Description
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* Filed herewith

** Furnished herewith

**TILE SHOP HOLDINGS, INC.
14000 Carlson Parkway
Plymouth, Minnesota 55441**

January 28, 2016

Lynda Stout
PO Box 79048
Charlotte, NC 28271

Dear Lynda:

I am delighted to offer you a position at Tile Shop Holdings, Inc. (the "Company"). This letter serves to confirm the terms of our offer of employment:

Position: Senior Vice President – Retail Stores

Start date: February 29, 2016

Status: Full-time, Regular

Reporting to: Chris Homeister, CEO

Compensation: Base salary (annualized) of \$310,000, paid in accordance with the Company's normal payroll procedures.

Bonus: You should note that the Company may modify salaries and benefits from time to time as its Board of Directors or the Compensation Committee thereof deems necessary or appropriate, and all forms of compensation which are referred to in this offer letter are subject to applicable withholding and payroll taxes. The Bonus opportunity would be 50% of pay and it would be based on achieving Company-wide goals and personal goals and objectives, pro-rated for the partial year during which you are employed by the Company.

Benefits: You will be eligible to receive the Company's standard benefit package for employees of your level.

Stock Options: Subject to approval by the Company's Board of Directors, you will be granted options to purchase 100,000 shares of the Company's common stock. The exercise price of the options will be the fair market value of the Company's common stock as of the date of grant. These options will vest over a five-year period and will otherwise be subject to the terms of the Company's 2012 Equity Award Plan (the "Plan") and your Stock Option Agreement entered into pursuant thereto. The options will vest evenly over the course of 5 years at 20% per year. The options will have a 7-year life upon issuance.

Vacation: 3 weeks

Technology: A laptop, tablet, and cell phone of your choosing will be issued on your start date.

Re-Location Expenses: The Company will reimburse re-location related expenses directly to you. For large expenditures, please have them pre-approved by me first. At your election, the company will pay these expenses directly to a vendor of your choosing that will assist you in your move.

It is the expectation of the company that your permanent move to the Twin Cities will be completed 3 months following your start date.

If a copy of your Social Security Card is not already on file with the Company, please provide the Company with your Social Security Card when you execute and return this letter. We will make a copy of your card and it will be kept in your employee file for payroll purposes.

Please understand that your employment with the Company is for no specified period and constitutes "at-will" employment. As a result, you are free to resign at any time, for any reason or for no reason, with or without notice. Similarly, the Company is free to conclude its employment relationship with you at any time, with or without cause, and with or without notice. This offer of employment is valid for consideration by the candidate until Friday, January 29, 2016.

The Company reserves the right to conduct background investigations and/or reference checks on all of its potential employees. Your job offer, therefore, is contingent upon a clearance of such a background investigation and/or reference check, if any.

For purposes of federal immigration law, you will be required to provide to the Company documentary evidence of your identity and eligibility for employment in the United States, if you have not already done so. Such documentation must be provided to the Company within three (3) business days of your date of hire, or our employment relationship with you may be terminated.

Like all Company employees of your level, you will be required, as a condition of your employment with the Company, to sign the Company's Nondisclosure, Confidentiality, Assignment and Noncompetition Agreement, a copy of which is attached hereto as Exhibit A (the "Non-Competition and Non-Disclosure Agreement").

You agree that, during the term of your employment with the Company, you will not engage in any other employment, occupation, consulting or other business activity directly related to the business in which the Company is now involved or becomes involved during the term of your employment, nor will you engage in any other activities that conflict with your obligations to the Company.

To indicate your acceptance of our offer, please sign and date the attached Acceptance and Acknowledgement. This letter, along with the Company's Non-Competition and Non-Disclosure Agreement, set forth the terms of your employment with the Company and supersede any prior representations or agreements, whether written or oral. This letter may not be modified or amended except by a written agreement, signed by an Officer of the Company and by you.

Lynda, I am looking forward to your arrival and expect your direct contributions to have a significant positive impact on the organization.

Kindest personal regards,

/s/ Chris Homeister

Chris Homeister, Chief Executive Officer
TILE SHOP HOLDINGS, INC.

**TILE SHOP HOLDINGS, INC.
14000 Carlson Parkway
Plymouth, Minnesota 55441**

ACCEPTANCE AND ACKNOWLEDGMENT

I accept the offer of employment from the Company as set forth in the offer letter dated January 28, 2016. I understand and acknowledge that my employment with the Company is for no particular duration and is at-will, meaning that I, or the Company, may terminate the employment relationship at any time, with or without cause and with or without prior notice. Additionally, I acknowledge that the Company reserves the right to conduct background investigations and/or reference checks on all of its potential employees, and that my job offer, therefore, is contingent upon a clearance of such a background investigation and/or reference check, if any.

I understand and agree that the terms and conditions set forth in the offer letter represent the entire agreement between the Company and me superseding all prior negotiations and agreements, whether written or oral. I understand that the terms and conditions described in the offer letter, along with the Company's Non-Competition and Non-Disclosure Agreement are the terms and conditions of my employment. No one other than an Officer of the Company is authorized to sign any employment or other agreement which modifies the terms of the offer letter and the Company's Non-Competition and Non-Disclosure Agreement, and any such modification must be in writing and signed by such individual. I understand that the Company may modify salary and benefits as well as other plans and programs from time to time as its Board of Directors or the Compensation Committee thereof deems necessary or appropriate.

Signature: /s/ Lynda W. Stout

Printed Name: Lynda Stout

Date: January 28, 2016

**TILE SHOP HOLDINGS, INC.
NONDISCLOSURE, CONFIDENTIALITY, ASSIGNMENT AND NONCOMPETITION AGREEMENT**

THIS NONDISCLOSURE, CONFIDENTIALITY, ASSIGNMENT AND NONCOMPETITION AGREEMENT (this "**Agreement**") is made this the 21st day of January 2016, by and between Tile Shop Holdings, Inc., a Delaware corporation and its subsidiaries (collectively with any predecessors, successors, and assignees, the "**Company**"), and Lynda Stout ("**I**" or "**me**"), to be effective on (the "**Effective Date**").

In consideration of my engagement or continued engagement as an officer, employee, director, advisor, partner, independent contractor or consultant of the Company (an "**Associate**"), and for other valuable consideration, the receipt and sufficiency of which is hereby acknowledged, I hereby agree as follows:

1. DEFINITIONS.

1.1. "**Affiliate**" means any direct or indirect subsidiary of the Company.

1.2. "**Confidential Information**" means any and all confidential and/or proprietary knowledge, data or information concerning the business, business relationships and financial affairs of the Company or its Affiliates whether or not in writing and whether or not labeled or identified as confidential or proprietary. By way of illustration, but not limitation, Confidential Information includes: (a) Inventions and (b) research and development activities of the Company or its Affiliates, services and marketing plans, business plans, budgets and unpublished financial statements, licenses, prices and costs, customer and supplier information and information disclosed to the Company or its Affiliates or to me by third parties of a proprietary or confidential nature or under an obligation of confidence. Confidential Information is contained in various media, including without limitation, patent applications, computer programs in object and/or source code, flow charts and other program documentation, manuals, plans, drawings, designs, technical specifications, laboratory notebooks, supplier and customer lists, internal financial data and other documents and records of the Company or its Affiliates.

1.3. "**Inventions**" means all ideas, concepts, discoveries, inventions, developments, improvements, formulations, products, processes, know-how, designs, formulas, methods, developmental or experimental work, clinical data, original works of authorship, software programs, software and systems documentation, trade secrets, technical data, or licenses to use (whether or not patentable or registrable under copyright or similar statutes), that are or were made, conceived, devised, invented, developed or reduced to practice or tangible medium by me, either alone or jointly with others (a) during any period that I am an Associate of the Company, whether or not during normal working hours or on the premises of the Company, which relate, directly or indirectly, to the business of the Company or its Affiliates, (b) at the request of or for the benefit of the Company during any period prior to my engagement as an Associate of the Company which relate, directly or indirectly, to the business of the Company or its Affiliates, or (c) which arise out of, or are incidental to, my engagement as an Associate of the Company.

1.4. "**Prior Inventions**" means any inventions made, conceived, devised, invented, developed or first reduced to practice by me, under my direction or jointly with others prior to the date of this Agreement and which do not constitute Inventions within the meaning of Section 1.3 above.

1.5. "**Third Party Information**" means any confidential or proprietary information received by the Company or its Affiliates from third parties.

2. CONFIDENTIALITY.

2.1. Recognition of the Company's Rights. I understand that the Company continually obtains and develops valuable Confidential Information which may or has become known to me in connection with my engagement as an Associate of the Company. I acknowledge that all Confidential Information is and shall remain the exclusive property of the Company or the third party providing such Confidential Information to myself, the Company, or the Company's Affiliates.

2.2. Nondisclosure of Confidential Information. I agree that during the term of my engagement as an Associate of the Company and thereafter, I will hold in strictest confidence and will not disclose, use, lecture upon, publish or otherwise make available to any third party (other than personnel of the Company or its Affiliates who need to know such information in connection with their work for the Company), any Confidential Information of the Company, except as such disclosure, use or publication may be required in connection with my work for the Company, or as expressly authorized in writing by an executive officer of the Company. I agree that I shall use such Confidential Information only in the performance of my duties for the Company and in accordance with any Company policies with respect to the protection of Confidential Information. I agree not to use such Confidential Information for my own benefit or for the benefit of any other person or business entity.

2.3. Third Party Information. In addition, I understand that the Company has received and in the future will receive Third Party Information subject to a duty on the Company's part to maintain the confidentiality of such information and to use it only for certain limited purposes. During the term of my engagement as an Associate of the Company and thereafter, I will hold Third Party Information in the strictest confidence and will not disclose to anyone (other than personnel of the Company or its Affiliates who need to know such information in connection with the performance of their duties for the Company) or use any Third Party Information, except as such disclosure or use may be required in connection with the performance of my duties for the Company, or as expressly authorized in writing by an executive officer of the Company.

2.4. Exceptions. My obligations under Sections 2.2 and 2.3 hereof shall not apply to the extent that certain Confidential Information: (a) is or becomes generally known within the Company's industry through no fault of mine; (b) was known to me at the time it was disclosed as evidenced by my written records at the time of disclosure; (c) is lawfully and in good faith made available to me by a third party who did not derive it from the Company or the Company's Affiliates and who imposes no obligation of confidence to me, the Company, or the Company's Affiliates; or (d) is required to be disclosed by a governmental authority or by order of a court of competent jurisdiction, provided that such disclosure is subject to all applicable governmental or judicial protection available for like material and reasonable advance notice is given to the Company.

2.5. Protection and Return of Confidential Information. I agree to exercise all reasonable precautions to protect the integrity and confidentiality of Confidential Information in my possession and not to remove any materials containing Confidential Information from the premises of the Company, except to the extent necessary in the performance of my duties for the Company or unless expressly authorized in writing by an executive officer of the Company. Upon the termination of my engagement as an Associate of the Company, or at any time upon the Company's request, I shall return immediately to the Company any and all notes, memoranda, specifications, devices, formulas and documents, together with copies thereof, and any other material containing or disclosing any Confidential Information of the Company or Third Party Information then in my possession or under my control.

3. ASSIGNMENT OF INVENTIONS.

3.1. Ownership of Inventions. I acknowledge that all Inventions already existing at the date of this Agreement or which arise after the date of this Agreement, belong to and are the absolute property of the Company and will not be used by me for any purpose other than carrying out my duties as an Associate of the Company.

3.2. Assignment of Inventions; Enforcement of Rights. Subject to Section 3.6, I hereby assign and agree to assign in the future to the Company all of my right, title and interest to any and all Inventions and any and all related patent rights, copyrights and applications and registrations therefore. I also agree to assign all my right, title and interest in and to any particular Inventions to a third party as directed by the Company. During and after my engagement as an Associate of the Company, I shall cooperate with the Company, at the Company's expense, in obtaining proprietary protection for the Inventions and I shall execute all documents which the Company shall reasonably request in order to perfect the Company's rights in the Inventions. I hereby appoint the Company my attorney to execute and deliver any such documents on my behalf in the event I should fail or refuse to do so within a reasonable period following the Company's request. I understand that, to the extent this Agreement shall be construed in accordance with the laws of any country or state which limits the assignability to the Company of certain inventions, this Agreement shall be interpreted not to apply to any such invention which a court rules or the Company agrees is subject to such limitation.

3.3. Works for Hire. I acknowledge that all original works of authorship made by me (solely or jointly with others) within the scope of my engagement as an Associate of the Company or any prior engagement by the Company, which are protectable by copyright are intended to be “works made for hire”, as that term is defined in Section 101 of the United States Copyright Act of 1976 (the “Act”), and shall be the property of the Company and the Company shall be the sole author within the meaning of the Act. If the copyright to any such copyrightable work shall not be the property of the Company by operation of law, I will, without further consideration, assign to the Company all of my right, title and interest in such copyrightable work and will cooperate with the Company and its designees, at the Company’s expense, to secure, maintain and defend for the Company’s benefit copyrights and any extensions and renewals thereof on any and all such work. I hereby waive all claims to moral rights in any Inventions.

3.4. Records. I agree to keep and maintain adequate and current records (in the form of notes, sketches, drawings and in any other form that may be required by the Company) of all Inventions made by me during the period of my engagement as an Associate of the Company or any prior engagement by the Company, which records shall be available to and remain the sole property of the Company at all times.

3.5. Obligation to Keep Company Informed. During the period of my engagement as an Associate of the Company, and for six (6) months after termination of my engagement as an Associate of the Company, I agree to promptly disclose to the Company fully and in writing all Inventions authored, conceived or reduced to practice by me, either alone or jointly with others. In addition, I will promptly disclose to the Company all patent applications filed by me or on my behalf within a year after termination of my engagement as an Associate of the Company.

3.6. Prior Inventions. I further represent that the attached Schedule A contains a complete list of all Prior Inventions. Such Prior Inventions are considered to be my property or the property of third parties and are not assigned to the Company hereunder. If there is no such Schedule A attached hereto, I represent that there are no such Prior Inventions. If I am claiming any Prior Inventions on Schedule A, I agree that, if in the course of my engagement as an Associate of the Company or any prior engagement by the Company, I incorporate any Prior Invention into a Company product, process or machine, the Company shall automatically be granted and shall have a non-exclusive, royalty-free, irrevocable, transferable, perpetual, world-wide license (with rights to sublicense) to make, have made, modify, use and sell such Prior Invention as part of, or in connection with, such product, process or machine. Notwithstanding the foregoing, I agree that I will not incorporate, or permit to be incorporated, Prior Inventions in any Company Inventions without the Company’s prior written consent.

4. OTHER AGREEMENTS.

4.1. No Conflicting Obligations. I hereby represent to the Company that, except as identified on Schedule B, I am not bound by any agreement or any other previous or existing business relationship which conflicts with or prevents the full performance of my duties and obligations to the Company (including my duties and obligations under this or any other agreement with the Company) during my engagement as an Associate of the Company. I agree I will not enter into, any agreement either written or oral that conflicts with this Agreement.

4.2. No Improper Use of Information of Prior Employers or Others. I understand that the Company does not desire to acquire from me any trade secrets, know-how or confidential business information I may have acquired from others. Therefore, I agree during my engagement as an Associate of the Company, I will not improperly use or disclose any proprietary information or trade secrets of any former or concurrent employer, or any other person or entity with whom I have an agreement or to whom I owe a duty to keep such information in confidence. Those persons or entities with whom I have such agreements or to whom I owe such a duty are identified on Schedule B.

5. **NON-COMPETITION.** I agree that while I am engaged as an Associate of the Company and for a period of one (1) year after termination or cessation of such engagement for any reason, I shall not, without the Company’s prior written consent, directly or indirectly, as a principal, employee, consultant, partner, or stockholder of, or in any other capacity with, any business enterprise (other than in my capacity as a holder of not more than 1% of the combined voting power of the outstanding stock of a publicly held company) (a) engage in direct or indirect competition with the Company or its Affiliates, (b) conduct a business of the type or character engaged in by the Company or its Affiliates at the time of termination or cessation of my engagement as an Associate of the Company, or (c) develop products or services competitive with those of the Company or its Affiliates.

6. GENERAL NON-SOLICITATION. I agree that while I am engaged as an Associate of the Company and for a period of one (1) year after termination or cessation of such engagement for any reason, I shall not solicit, divert or take away, or attempt to divert or take away, the business or patronage of any of the clients, customers or accounts, or prospective clients, customers or accounts, of the Company or its Affiliates which were contacted, solicited or served by me while I was engaged as an Associate of the Company or any Affiliate.

7. NON-SOLICITATION OF EMPLOYEES AND CONSULTANTS. I agree that while I am engaged as an Associate of the Company and for a period of one (1) year after termination or cessation of such engagement for any reason, I shall not directly or indirectly hire, recruit, or solicit any employee, independent contractor or consultant of the Company or its Affiliates, or induce or attempt to induce any employee independent contractor or consultant of the Company or its Affiliates to discontinue his or her relationship with the Company or its Affiliates.

8. NOTICE OF SUBSEQUENT EMPLOYMENT OR ENGAGEMENT. I shall, for a period of one (1) year after the termination or cessation of my engagement as an Associate of the Company, notify the Company of any change of address, and of any subsequent employment or engagement (stating the name and address of the employer and the nature of the position) or any other business activity.

9. GENERAL.

9.1. Assignment, Successors and Assigns. This Agreement may not be assigned by either party except that the Company may assign this Agreement to any Affiliate or in connection with the merger, consolidation or sale of all or substantially all of its business or assets. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective successors and other legal representatives and, to the extent that any assignment hereof is permitted hereunder, their assignees.

9.2. Entire Agreement. The obligations pursuant to Sections 2 and 3 of this Agreement shall apply to any time during which I was previously engaged as an Associate of the Company, or am in the future engaged as an Associate of the Company or any Affiliate if no other agreement governs nondisclosure and assignment of inventions during such period. This Agreement supersedes all prior agreements, written or oral, with respect to the subject matter of this Agreement.

9.3. Severability. In the event that any one or more of the provisions contained herein shall, for any reason, be held to be invalid, illegal, or unenforceable in any respect, such invalidity, illegality, or unenforceability shall not affect any other provisions of this Agreement, and all other provisions shall remain in full force and effect. If any of the provisions of this Agreement is held to be excessively broad, it shall be reformed and construed by limiting and reducing it so as to be enforceable to the maximum extent permitted by law. I agree that should I violate any obligation imposed on me in this Agreement, I shall continue to be bound by the obligation until a period equal to the term of such obligation without violation of such obligation.

9.4. Amendments and Waivers. No modification of or amendment to this Agreement, nor any waiver of any rights under this Agreement, will be effective unless in writing and signed by the party to be charged. No delay or omission by the Company in exercising any right under this Agreement will operate as a waiver of that or any other right. A waiver or consent given by the Company on any occasion is effective only in that instance and will not be construed as a bar to or waiver of any right on any other occasion.

9.5. Employment. I understand that this Agreement does not constitute a contract of employment or create an obligation on the part of the Company to continue my employment (if any) with the Company. I understand that my employment (if any) is "at will" and that my obligations under this Agreement shall not be affected by any change in my position, title or function with, or compensation, by the Company. Any subsequent change or changes in my duties, salary or compensation will not affect the validity or scope of this Agreement.

9.6. Legal and Equitable Remedies. I acknowledge that (a) the business of the Company and its Affiliates is global in scope and its services may be marketed and sold throughout the world; (b) the Company and its Affiliates compete with other businesses that are or could be located in any part of the world; (c) the Company has required that I make the covenants contained in this Agreement as a condition to my engagement as an Associate of

the Company; and (d) the restrictions contained in this Agreement are necessary for the protection of the business and goodwill of the Company and its Affiliates and are reasonable for such purpose. I agree that any breach of this Agreement by me will cause irreparable damage to the Company and its Affiliates and that in the event of such breach, the Company shall be entitled, in addition to monetary damages and to any other remedies available to the Company under this Agreement and at law, to equitable relief, including injunctive relief, and to payment by myself of all costs incurred by the Company in enforcing of the provisions of this Agreement, including reasonable attorneys' fees. I agree that should I violate any obligation imposed on me in this Agreement, I shall continue to be bound by the obligation until a period equal to the term of such obligation has expired without violation of such obligation.

9.7. Governing Law. This Agreement shall be construed as a sealed instrument and shall in all events and for all purposes be governed by, and construed in accordance with, the laws of the State of Delaware without regard to any choice of law principle that would dictate the application of the laws of another jurisdiction. Any action, suit or other legal proceeding which I may commence to resolve any matter arising under or relating to any provision of this Agreement shall be commenced only in a court of the State of Delaware (or, if appropriate, a federal court located within the State of Delaware), and I hereby consent to the jurisdiction of such court with respect to any action, suit or proceeding commenced in such court by the Company.

[Next Page is Signature Page]

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written as an instrument under seal.

EMPLOYEE

/s/ Lynda W. Stout
Lynda Stout

TILE SHOP HOLDINGS, INC.

By: /s/ Chris Homeister
Name: Chris Homeister
Title: Chief Executive Officer

Schedule A

List all Prior Inventions

Schedule B

List any and all Conflicted Obligations

TILE SHOP HOLDINGS, INC.

Subsidiaries of the Company (all of which are 100% owned, either directly or indirectly)

The Tile Shop, LLC, a Delaware limited liability company

The Tile Shop of Michigan, LLC, a Michigan limited liability company

The Tile Shop of Oklahoma, LLC, a Delaware limited liability company

Tile Shop Lending, Inc., a Delaware corporation

The Tile Shop (Beijing) Trading Company Ltd., a Chinese limited liability company

CERTIFICATIONS

I, Chris R. Homeister, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Tile Shop Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: April 28, 2016

/s/ CHRIS R. HOMEISTER
Chris R. Homeister
Chief Executive Officer

CERTIFICATIONS

I, Kirk L. Geadelmann, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Tile Shop Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: April 28, 2016

/s/ KIRK L. GEADELMANN
Kirk L. Geadelmann
Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Tile Shop Holdings, Inc. (the "Company") on Form 10-Q for the period ending March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Chris R. Homeister, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

/s/ CHRIS R. HOMEISTER

Chris R. Homeister
Chief Executive Officer

April 28, 2016

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

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Tile Shop Holdings, Inc. (the "Company") on Form 10-Q for the period ending March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Kirk L. Gadelmann, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

/s/ KIRK L. GEADELMANN

Kirk L. Gadelmann
Chief Financial Officer

April 28, 2016

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