

TILE SHOP HOLDINGS, INC.
Form POS AM
November 16, 2012

As filed with the Securities and Exchange Commission on November 16, 2012

File No. 333-182482

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

POST-EFFECTIVE AMENDMENT NO. 3

ON

FORM S-1

TO

REGISTRATION STATEMENT on FORM S-4 (FILE NO. 333-182482)

Under

The Securities Act of 1933

TILE SHOP HOLDINGS, INC.

(Exact name of Registrant as specified in its charter)

Delaware	5713	45-5538095
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

14000 Carlson Parkway

Plymouth, Minnesota 55441

(763) 852-2901

(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)

Robert A. Rucker
Chief Executive Officer
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(763) 852-2901

with a copy to:
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Approximate date of commencement of the proposed sale to the public: From time to time after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box "

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

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

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐ (Do not check if a smaller reporting company)

Smaller reporting company ☐

EXPLANATORY NOTE

This Post-Effective Amendment No. 3 on Form S-1 to the Registration Statement on Form S-4 (File No. 333-182482) relates to the public offering of common stock of the registrant upon exercise of certain warrants, as contemplated by the Registration Statement on Form S-4 (File No. 333-182482) (the “Prior Registration Statement”), and is being filed in order to maintain the effectiveness of the Prior Registration Statement to the extent that such Prior Registration Statement pertains to the shares of the registrant’s common stock issuable upon exercise of such warrants.

The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED NOVEMBER 16, 2012

PROSPECTUS

12,500,000 Shares

TILE SHOP HOLDINGS, INC.

Common Stock

This prospectus relates to the issuance by us of up to 12,500,000 shares of our common stock, par value \$0.0001 per share, upon the exercise of warrants that were originally issued by JWC Acquisition Corp., a Delaware corporation (“JWCAC”), in connection with its initial public offering and that became exercisable for shares of our common stock upon the consummation of the transactions contemplated by that certain Contribution and Merger Agreement (the “Business Combination”), dated as of June 27, 2012, by and among JWCAC, on the one hand, and The Tile Shop, LLC, a Delaware limited liability company (“The Tile Shop”), the members of The Tile Shop (the “Members”), Nabron International Inc., a Bahamas corporation (“Nabron” and, together with the Members other than ILTS, LLC the “Sellers”), Tile Shop Holdings, Inc., a Delaware corporation (the “Company”), Tile Shop Merger Sub, Inc., Delaware corporation and wholly owned subsidiary of TS Holdings, and Peter Jacullo, in his capacity as Sellers’ Representative, on the other hand, at an exercise price of \$11.50 per share (each, a “Public Warrant” and collectively, the “Public Warrants”).

Each Warrant entitles the holder thereof to purchase one share of our common stock upon payment of the exercise price of \$11.50 per share. We will receive the proceeds from the exercise of the Public Warrants, but not from the sale of the underlying shares of common stock.

Our common stock is listed on The NASDAQ Global Market under the symbol “TTS.” The Public Warrants are quoted on the Over-the-Counter Bulletin Board under the symbol “TTSAW.” On November 12, 2012, the closing sale prices of our common stock and Public Warrants were \$13.69 and \$3.27, respectively.

Investing in our common stock involves risks that are described in the “Risk Factors” section beginning on page 11 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the securities to be issued under this prospectus or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is _____, 2012.

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You should rely only on the information contained or incorporated by reference in this prospectus. No one has been authorized to provide you with information that is different from that contained or incorporated by reference in this prospectus. This prospectus is dated as of the date set forth on the cover hereof. You should not assume that the information contained in this prospectus is accurate as of any date other than that date. You should not assume that the information incorporated by reference in this prospectus is accurate as of any date other than the date of such incorporated document.

INFORMATION CONCERNING FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements within the meaning of the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. In some cases you can identify these statements by forward-looking words such as “may,” “might,” “will,” “will likely result,” “should,” “anticipates,” “expects,” “intends,” “plans,” “seeks,” “estimates,” “continue,” “believes” and similar expressions, although some forward-looking statements are expressed differently.

These forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties that may cause our actual results, performance, or achievements to differ materially from any expected future results, performance, or achievements expressed or implied by such forward-looking statements. All statements other than statements of historical fact are statements that could be deemed forward-looking statements. These risks and uncertainties include, but are not limited to:

- the level of demand for our products;
- our ability to grow and remain profitable in the highly competitive retail tile industry;
- our ability to access additional capital;
- our ability to attract and retain qualified personnel;
- changes in general economic, business and industry conditions;
- our ability to introduce new products that satisfy market demand; and
- legal, regulatory, and tax developments, including additional requirements imposed by changes in domestic and foreign laws and regulations.

There is no assurance that our expectations will be realized. If one or more of these risks or uncertainties materialize, or if our underlying assumptions prove incorrect, actual results may vary materially from those expected, estimated, or projected. Such risks and uncertainties also include those set forth under “Risk Factors” herein. Our forward-looking statements speak only as of the time that they are made and do not necessarily reflect our outlook at any other point in time. Except as required by law or regulation, we undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events, or for any other reason.

PROSPECTUS SUMMARY

This summary highlights information contained elsewhere in this prospectus and does not contain all of the information that you should consider in making your investment decision. Before investing in our securities, you should carefully read this entire prospectus, including our consolidated financial statements and the related notes included in this prospectus and the information set forth under the headings “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Unless the context requires otherwise, the words “Tile Shop Holdings,” “we,” “company,” “us,” and “our” refer to Tile Shop Holdings, Inc. and our consolidated subsidiaries.

Overview

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. We sell over 4,000 products from around the world, including ceramic, porcelain, glass, and stainless steel manufactured tiles and, marble, granite, quartz, sandstone, travertine, slate, and onyx natural tiles, primarily under our proprietary Rush River, Fired Earth, and Superior brand names. We purchase our tile products and accessories directly from producers and manufacture our own setting and maintenance materials, such as thinset, grout, and sealers. We operate 62 stores in 20 states, with an average size of 23,000 square feet. We also sell our products on our website.

We believe that our long-term producer 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, 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 stone tiles, accessories, and related materials in the United States.

In 2011, we reported net sales and income from operations of \$152.7 million and \$32.6 million, respectively. From December 31, 2007 to December 31, 2011, our net sales and income from operations increased at compounded annual growth rates of 8.2% and 14.0%, respectively. During that period, our growth was driven by a combination of opening 14 new retail locations and an increase in same store sales. We have opened nine new stores in 2012 and intend to open an additional four stores during the remainder of 2012 and no fewer than 15 stores in 2013.

Competitive Strengths

We believe that the following factors differentiate us from our competitors and position us to continue to grow our specialty tile business.

Inspiring Customer Experience. Our showrooms bring our products to life. Each showroom features up to 60 different mockups, or vignettes, of bathrooms, kitchens, fireplaces, foyers, and other settings that showcase our broad array of products. Each store also features over 1,400 hand-crafted display boards showing tile that we offer for sale. Our stores are spacious, well-lit, and organized by product type to make our customers' shopping experience easy.

Broad Product Assortment at Attractive Prices. We offer over 4,000 manufactured and natural tile products, setting and maintenance materials, and accessories. We are able to maintain every-day low prices by purchasing tile and accessories directly from producers and manufacturing our own setting and maintenance materials.

Customer Service and Satisfaction. Our sales personnel are highly-trained and knowledgeable about the technical and design aspects of our products. We offer weekly do-it-yourself classes in all of our showrooms. In addition, we provide one-on-one installation training, as required, to meet customer needs. We offer a liberal return policy, with no restocking fees.

Worldwide Sourcing Capabilities. We have long-standing relationships with producers of our tiles throughout the world and work with them to design products exclusively for us. We believe that these direct relationships differentiate us from our competitors, who generally purchase commodity products through distributors. We are often the largest or exclusive customer for many of our producers.

Proprietary Branding. We sell the majority of our products under our proprietary brand names, which helps us to differentiate our products from those of our competitors. We offer products across a range of price points and quality levels that allow us to target discrete market segments and to appeal to diverse groups of customers.

Centralized Distribution System. We service our retail locations from three distribution centers. Our distribution centers can cost-effectively service stores within a 700-mile radius, providing us with the ability to open new locations in markets where we believe that we have a competitive advantage or see attractive demographics.

Experienced Team . Our management team has substantial experience in the specialty tile industry and retail sales operations. Robert Rucker, our founder and chief executive officer, has over 25 years of experience in the tile industry. Both Carl Randazzo, senior vice president—retail, and Joseph Kinder, senior vice president—operations, have been with us for over 20 years. William Watts, who serves as the chairman of our board of directors, is the former chief executive officer of General Nutrition Corporation, the chairman of Mattress Firm, Inc. and a director of Brookstone, Inc.

Historically Attractive Returns on New Store Investment. Our new stores have historically begun generating operating profit within the first year of operations and we generally recoup our initial net capital investment from a new store's four-wall profitability within the first 36 months of operations. We measure four-wall profitability as store level operating profit before pre-opening costs and depreciation and amortization.

Growth Strategy

We intend to increase our net sales and profitability through a combination of new store openings and same store sales growth. In the five years ended December 31, 2011, we grew through a combination of opening 20 new retail locations and increases in same store sales. We expect to continue to gain market share. Specific elements of our strategy for continued growth include the following:

Open New Stores . We believe that the highly-fragmented U.S. retail tile market provides us with a significant opportunity to expand our store base. Since January 1, 2012, we have opened nine new stores and plan to open an

additional four stores during the remainder of 2012. We intend to open no fewer than 15 new stores in 2013, primarily in our existing markets and the mid-Atlantic, southeastern, and southern New England regions of the United States. We believe that there will continue to be additional expansion opportunities in the United States and Canada. We expect our store base growth to increase operational efficiencies.

Increase Sales and Profitability of Existing Stores. We believe that our ongoing investment in new products and our enhanced training program for our sales associates, together with our associate incentive compensation structure, will result in continued same store sales growth.

Risk Factors

Our business is subject to numerous risks and uncertainties, including those highlighted in the section entitled “Risk Factors” immediately following this prospectus summary, that represent challenges that we face in connection with the successful implementation of our strategy and the growth of our business.

Corporate Information

We were incorporated in the State of Delaware in June 2012 in order to become the parent company of The Tile Shop, LLC, or The Tile Shop, following the consummation of a business combination, or the Business Combination, with JWC Acquisition Corp., or JWCAC, a blank check company incorporated in the State of Delaware in July 2010. On August 21, 2012, we consummated the Business Combination and, in connection therewith, became a successor issuer to JWCAC by operation of Rule 12g-3(a) promulgated under the Securities Exchange Act of 1934, as amended, or the Exchange Act.

Our principal executive offices are located at 14000 Carlson Parkway, Plymouth, Minnesota, 55441, and our telephone number is (763) 852-2901. Our website address is www.tileshop.com. We had approximately 744 employees as of September 30, 2012. Information contained on our website is not a part of this prospectus and the inclusion of our website address in this prospectus is an inactive textual reference only.

SUMMARY CONSOLIDATED FINANCIAL AND OTHER DATA

The following table sets forth selected historical financial information derived from (i) our unaudited financial statements included elsewhere in this prospectus as of and for the nine months ended September 30, 2012 and 2011, (ii) The Tile Shop's audited financial statements included elsewhere in this prospectus as of December 31, 2011 and 2010 and for the years ended December 31, 2011, 2010 and 2009 and (iii) The Tile Shop's audited financial statements not included in this report as of December 31, 2009, 2008 and 2007 and for the years ended December 31, 2008 and 2007. You should read the following selected financial data in conjunction with the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the financial statements and the related notes appearing elsewhere in this prospectus.

	As of September 30, or for the nine months ended September 30,		As of December 31, or for the year ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
Statement of Income Data							
Net sales	\$ 136,463	\$ 115,015	\$ 152,717	\$ 135,340	\$ 116,247	\$ 118,960	\$ 111,607
Cost of sales	37,025	30,298	40,321	36,124	31,706	34,001	33,588
Gross profit	99,438	84,717	112,396	99,216	84,541	84,959	78,019
Selling, general and administrative expenses	68,606	58,225	78,368	68,105	60,051	61,322	58,539
Deferred compensation expense	3,897	966	1,415	450	120	260	150
Income from operations	26,935	25,526	32,613	30,661	24,370	23,377	19,330
Interest expense	626	297	443	467	545	592	972
Other income (expense)	23	36	(77)	(810)	(1,017)	(509)	(1,381)
Income before income taxes	26,332	25,265	32,093	30,318	23,898	23,460	18,921
Benefit (provision) for income taxes (1)	4,299	(578)	(733)	(609)	(675)	(724)	(461)
Net income	\$ 30,631	\$ 24,687	\$ 31,360	\$ 29,709	\$ 23,223	\$ 22,736	\$ 18,460
Earnings per share (1)	\$ 0.91	\$ 0.77	\$ 0.97	\$ 0.92	\$ 0.72	\$ 0.70	\$ 0.57
	33,544	32,000	32,261	32,330	32,330	32,330	32,330

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Weighted
average share
outstanding
Balance Sheet
Data

Cash and cash equivalents	\$ 5,960	\$ 12,253	\$ 6,283	\$ 14,117	\$ 17,850	\$ 3,631	\$ 638
Inventories	40,662	42,704	43,744	35,358	26,342	28,046	22,891
Total assets	161,830	122,512	119,005	108,890	95,632	80,225	78,802
Total debt and capital lease obligations, including current maturities	73,226	4,964	4,853	5,582	4,574	5,035	6,334
Total stockholders' equity	42,306	81,492	75,147	69,437	62,000	49,586	39,084
Working capital	28,880	42,347	34,852	34,895	31,851	18,949	9,980

Cash Flow
Data

Net cash provided by operating activities	\$ 41,540	\$ 23,597	\$ 34,723	\$ 32,461	\$ 34,729	\$ 25,156	\$ 27,885
Net cash used in investing activities	(17,187)	(11,372)	(18,561)	(14,376)	(8,267)	(9,435)	(12,928)
Net cash used in financing activities	(24,676)	(14,089)	(23,994)	(21,819)	(12,243)	(12,728)	(14,330)

Other Selected
Financial Data
(unaudited)

Adjusted EBITDA ⁽²⁾	\$ 38,662	\$ 32,687	\$ 42,602	\$ 38,472	\$ 31,576	\$ 30,818	\$ 25,832
Adjusted EBITDA margin ⁽²⁾	28.3 %	28.4 %	27.9 %	28.4 %	27.2 %	25.9 %	23.1 %
Gross margin ⁽³⁾	72.9 %	73.7 %	73.6 %	73.3 %	72.7 %	71.4 %	69.9 %
Operating income margin ⁽⁴⁾	19.7 %	22.2 %	21.4 %	22.7 %	21.0 %	19.7 %	17.3 %
Same stores sales growth ⁽⁵⁾	5.5 %	6.1 %	6.4 %	11.4 %	(4.6)%	(3.4)%	3.4 %

(1) Historical amounts do not include pro forma adjustments for income taxes as a result of The Tile Shop's change in tax status, which was effective on August 21, 2012.

(2) We calculate Adjusted EBITDA by taking net income calculated in accordance with accounting principles generally accepted in the United States, or GAAP, and adding interest expense, income taxes, depreciation and amortization, deferred compensation, and stock-based compensation. Adjusted EBITDA margin is equal to Adjusted EBITDA divided by net sales. 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 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.

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 limitation of these non-GAAP financial measures is that they exclude significant expenses and income that are required by GAAP to be recorded 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.

	Nine Months Ended September 30,		Years Ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
Net Income	\$ 30,631	\$ 24,687	\$ 31,360	\$ 29,709	\$ 23,223	\$ 22,736	\$ 18,460
Interest expense	626	297	443	467	545	592	972
Income taxes	(4,299)	579	733	609	675	724	461
Depreciation and amortization	7,543	6,158	8,651	7,237	7,013	6,506	5,789
Deferred compensation expense	3,898	966	1,415	450	120	260	150
Stock-based compensation	263	-	—	—	—	—	—
Adjusted EBITDA	\$ 38,662	\$ 32,687	\$ 42,602	\$ 38,472	\$ 31,576	\$ 30,818	\$ 25,832

(3) Gross margin is gross profit divided by net sales.

(4) Operating income margin is income from operations divided by net sales.

(5) Same store sales growth is the percentage change in sales of comparable stores period over period. A store is considered comparable on the first day of the 13th month of operation. Same store sales growth amounts include total charges to customers less any actual returns. We do not include estimated return provisions or sale allowances in the same store sales calculation, as return reserves are calculated on a consolidated level, and the analysis does not include website sales. Same store sales data reported by other companies may be prepared on a different basis and therefore may not be useful for purposes of comparing our results to those of other businesses.

RISK FACTORS

An investment in our securities involves a high degree of risk. You should carefully consider the risks described below before making an investment decision. Our business, prospects, financial condition, or operating results could be harmed by any of these risks, as well as other risks not currently known to us or that we currently consider immaterial. The trading price of our securities could decline due to any of these risks, and, as a result, you may lose all or part of your investment.

Our business is dependent on general economic conditions in our markets.

Our revenues depend, in part, on discretionary spending by our customers. Pressure on discretionary income brought on by economic downturns and slow recoveries, including housing market declines, rising energy prices, and weak labor markets, may cause consumers to reduce the amount that they spend on discretionary items. If recovery from the current economic downturn continues to be slow or prolonged, our growth, prospects, results of operations, cash flows, and financial condition could be adversely impacted. General economic conditions and discretionary spending are beyond our control and are affected by, among other things:

- consumer confidence in the economy;
- unemployment trends;
- consumer debt levels;
- consumer credit availability;
- the housing market;
- gasoline and fuel prices;
- interest rates and inflation;
- price deflation, including due to low-cost imports;

- slower rates of growth in real disposable personal income;
- natural disasters;
- national security concerns;
- tax rates and tax policy; and
- other matters that influence consumer confidence and spending.

Increasing volatility in financial markets may cause some of the above factors to change with an even greater degree of frequency and magnitude than in the past.

Our ability to grow and remain profitable may be limited by direct or indirect competition in the retail tile industry, which is highly competitive.

The retail tile industry in the United States is highly competitive. Participants in the tile industry compete primarily based on product variety, customer service, store location, and price. There can be no assurance that we will be able to continue to compete favorably with our competitors in these areas. Our store competitors include large national home centers (such as Home Depot and Lowe's), regional and local specialty retailers of tile (such as Tile America, World of Tile, Century Tile, and Floor and Décor), factory direct stores (such as Dal-Tile and Florida Tile) and privately-owned, single-site stores. We also compete indirectly with companies that sell other types of floor coverings, including wood floors, carpet, and vinyl sheet. In the past, we have faced periods of heightened competition that materially affected our results of operations. Certain of our competitors have greater name recognition, longer operating histories, more varied product offerings, and substantially greater financial and other resources than us. Accordingly, we may face periods of intense competition in the future that could have a material adverse effect on our planned growth and future results of operations. In addition, the barriers to entry into the retail tile industry are relatively low. New or existing retailers could enter our markets and increase the competition that we face. In addition, manufacturers and vendors of tile and related products, including those whose products we currently sell, could enter the U.S. retail tile market and start directly competing with us. Competition in existing and new markets may also prevent or delay our ability to gain relative market share. Any of the developments described above could have a material adverse effect on our planned growth and future results of operations.

Our management and auditors have identified a material weakness in our internal controls over financial reporting that, if not properly remediated, could result in material misstatements in our financial statements.

Prior to the Business Combination, we were not required to comply with Section 404 of the Sarbanes-Oxley Act of 2002. As such, we did not make an assessment of the effectiveness of our internal controls over financial reporting nor did we engage our auditors to express, nor have our auditors expressed, an opinion on the effectiveness of our internal controls over financial reporting. In connection with the audit of our consolidated financial statements for the year ended December 31, 2011, our auditors informed us that they had identified a material weakness in our internal controls over financial reporting related to deficiencies in the financial statement close process. Under the standards established by the Public Company Accounting Oversight Board, a material weakness is a deficiency, or combination of deficiencies, in internal controls over financial reporting, such that there is a reasonable possibility that a material misstatement of annual or interim financial statements will not be prevented or detected and corrected on a timely basis. If we are unable to remediate our historical material weakness or if additional material weaknesses are identified in the future, a material weakness may exist in our internal controls over financial reporting.

The primary factors contributing to the material weakness in our financial statement close process were:

- We lacked sufficient personnel with requisite competencies within our finance function for a company of our size and complexity.

· We did not maintain financial close processes, procedures, and reporting systems that were adequately designed to support the accurate and timely reporting of our financial results.

During the quarter ended September 30, 2012, we hired a chief financial officer who initiated an analysis of our internal accounting controls and procedures. This process has resulted in a number of changes to our processes and procedures that have served to strengthen our controls over financial reporting. We have also taken steps to remedy the historical material weakness identified by our auditors in connection with their audit of our consolidated financial statements for the year ended December 31, 2011 by designing and implementing a formalized financial reporting process that includes: conducting properly prepared, supported, and reviewed balance sheet reconciliations; conducting properly prepared, supported, and reviewed journal entries; following a properly completed and approved financial close checklist; and abiding by a financial reporting calendar.

We plan to complete this remediation process as quickly as possible. However, we cannot at this time estimate how long it will take or if it can successfully remediate the historical material weakness. If we are unable to successfully remediate the historical weakness, we may be unable to produce accurate and timely financial statements. Any failure to timely provide required financial information could materially and adversely impact our financial condition and the market value of our securities.

If we fail to successfully manage the challenges that our planned growth poses or encounter unexpected difficulties during our expansion, our revenues and profitability could be materially adversely affected.

One of our long term objectives is to increase revenues and profitability through market share leadership. Our ability to achieve market share leadership, however, is contingent upon our ability to open new stores and achieve operating results in new stores at the same level as our similarly situated current stores. There can be no assurance that we will be able to open stores in new markets at the rate required to achieve market leadership in such markets, identify and obtain favorable store sites, arrange favorable leases for stores, or obtain governmental and other third-party consents, permits, and licenses needed to open or operate stores in a timely manner, train and hire a sufficient number of qualified managers for new stores, attract a strong customer base and brand familiarity in new markets, or successfully compete with established retail tile stores in the new markets that we enter. Failure to open new stores in an effective and cost-efficient manner could place us at a competitive disadvantage as compared to retailers who are more adept than us at managing these challenges, which, in turn, could negatively affect our overall operating results.

Our same store sales fluctuate due to a variety of economic, operating, industry and environmental factors and may not be a fair indicator of our overall performance.

Our same store sales have experienced fluctuations, which can be expected to continue. Numerous factors affect our same store sales results, including among others, the timing of new and relocated store openings, the relative proportion of new and relocated stores to mature stores, cannibalization resulting from the opening of new stores in existing markets, changes in advertising and other operating costs, the timing and level of markdowns, changes in our

product mix, weather conditions, retail trends, the retail sales environment, economic conditions, inflation, the impact of competition, and our ability to execute our business strategy efficiently. As a result, same store sales or operating results may fluctuate, and may cause the price of our securities to fluctuate significantly. Therefore, we believe that period-to-period comparisons of our same store sales may not be a fair indicator of our overall operating performance.

We intend to open additional stores in our existing markets, which may diminish sales by existing stores in those markets and strain our ability to find qualified personnel or divert our resources from our existing stores, negatively affecting our overall operating results.

Our expansion strategy includes plans to open additional stores in our existing markets as part of our plan to open four additional new stores in the remainder of 2012 and no fewer than 15 new stores in 2013. Because our stores typically draw customers from their local areas, additional stores may draw customers away from nearby existing stores and may cause same store sales performance at those existing stores to decline, which may adversely affect our overall operating results. In addition, our ability to open additional stores will be dependent on our ability to promote and/or recruit enough qualified field managers, store managers, assistant store managers, and sales associates. The time and effort required to train and supervise a large number of new managers and associates and integrate them into our culture may divert resources from our existing stores. If we are unable to profitably open additional stores in existing markets and limit the adverse impact of those new stores on existing stores, it may reduce our same store sales and overall operating results during the implementation of our expansion strategy.

Our expansion strategy will be dependent upon, and limited by, the availability of adequate capital.

Our expansion strategy will require additional capital for, among other purposes, opening new stores and entering new markets. Such capital expenditures will include researching real estate and consumer markets, lease, inventory, property and equipment costs, integration of new stores and markets into company-wide systems and programs, and other costs associated with new stores and market entry expenses and growth. If cash generated internally is insufficient to fund capital requirements, we will require additional debt or equity financing. Adequate financing may not be available or, if available, may not be available on terms satisfactory to us. In addition, our credit facility may limit the amount of capital expenditures that we may make annually, depending on our leverage ratio. If we fail to obtain sufficient additional capital in the future or we are unable to make capital expenditures under our credit facility, we could be forced to curtail our expansion strategies by reducing or delaying capital expenditures relating to new stores and new market entry. As a result, there can be no assurance that we will be able to fund our current plans for the opening of new stores or entry into new markets.

We depend on a number of suppliers, and any failure by any of them to supply us with products may impair our inventory and adversely affect our ability to meet customer demands, which could result in a decrease in revenues and/or gross margin.

Our current suppliers may not continue to sell products to us on acceptable terms or at all, and we may not be able to establish relationships with new suppliers to ensure delivery of products in a timely manner or on terms acceptable to us. We do not have long-term contractual supply agreements with our suppliers which obligate them to supply us with products at specified quantities or prices. We may not be able to acquire desired merchandise in sufficient quantities on terms acceptable to us in the future. We are also dependent on suppliers for assuring the quality of merchandise supplied to us. Our inability to acquire suitable merchandise in the future or the loss of one or more of our suppliers and our failure to replace them may harm our relationship with our customers and our ability to attract new customers, resulting in a decrease in net sales.

We source the approximately 4,000 products that we stock and sell from over 100 domestic and international vendors. We source a large number of those products from foreign manufacturers, including approximately 55% of our products from a group of 10 suppliers located primarily in Asia. We generally take title to these products overseas and are responsible for arranging shipment to our distribution centers. Financial instability among key vendors, political instability, trade restrictions, tariffs, currency exchange rates, and transport capacity and costs are beyond our control and could negatively impact our business if they seriously disrupt the movement of products through our supply chain or increased the costs of our products.

If our suppliers do not use ethical business practices or comply with applicable laws and regulations, our reputation could be harmed due to negative publicity and we could be subject to legal risk.

We do not control the operations of our suppliers. Accordingly, we cannot guarantee that our suppliers will comply with applicable environmental and labor laws and regulations or operate in a legal, ethical, and responsible manner. Violation of environmental, labor or other laws by our suppliers or their failure to operate in a legal, ethical, or responsible manner, could reduce demand for our products if, as a result of such violation or failure, we attract negative publicity. Further, such conduct could expose us to legal risks as a result of the purchase of products from non-compliant suppliers.

If customers are unable to obtain third-party financing at satisfactory rates, sales of our products could be materially adversely affected.

Our business, financial condition, and results of operations have been, and may continue to be affected, by various economic factors. Deterioration in the current economic environment could lead to reduced consumer and business spending, including by our customers. It may also cause customers to shift their spending to products that we either do not sell or that generate lower profitability for us. Further, reduced access to credit may adversely affect the ability of consumers to purchase our products. This potential reduction in access to credit may adversely impact our ability to offer customers credit card financing through third party credit providers on terms similar to those offered currently, or at all. In addition, economic conditions, including decreases in access to credit, may result in financial difficulties leading to restructuring, bankruptcies, liquidations and other unfavorable events for our customers, which may adversely impact our industry, business, and results of operations.

Any failure by us to successfully anticipate consumer trends may lead to loss of consumer acceptance of our products, resulting in reduced revenues.

Our success depends on our ability to anticipate and respond to changing trends and consumer demands in a timely manner. If we fail to identify and respond to emerging trends, consumer acceptance of our merchandise and our image with current or potential customers may be harmed, which could reduce our revenues. Additionally, if we misjudge market trends, we may significantly overstock unpopular products and be forced to reduce the sales price of such products, which would have a negative impact on our gross profit and cash flow. Conversely, shortages of products that prove popular could also reduce our revenues.

We depend on a few key employees, and if we lose the services of certain of our executive officers, we may not be able to run our business effectively.

Our future success depends in part on our ability to attract and retain key executive, merchandising, marketing, and sales personnel. Our executive officers include Robert Rucker, president and chief executive officer; Carl Randazzo, senior vice president—retail; and Joseph Kinder, senior vice president—operations. We have employment and non-compete arrangements with each of Messrs. Rucker, Randazzo, and Kinder. If any of these executive officers ceases to be employed by us, we would have to hire additional qualified personnel. Our ability to successfully hire other experienced and qualified executive officers cannot be assured, and may be difficult because we face competition for these professionals from our competitors, our suppliers and other companies operating in our industry. As a result, the loss or unavailability of any of our executive officers could have a material adverse effect on us.

We have entered into a \$100 million credit facility. The burden of this additional debt could adversely affect us, make us more vulnerable to adverse economic or industry conditions, and prevent us from fulfilling our debt obligations or from funding our expansion strategy.

In connection with the Business Combination, we issued promissory notes in an aggregate principal amount of approximately \$70 million. We have entered into a credit facility with Bank of America, N.A., as administrative agent and The Huntington National Bank, as syndication agent, for \$100 million, including a term loan of \$25 million and a revolving credit facility of \$75 million, which we have used, in part, to repay the promissory notes issued in connection with the Business Combination. The terms of our credit facility and the burden of the indebtedness incurred thereunder could have serious consequences for us, such as :

- limiting our ability to obtain additional financing to fund our working capital, capital expenditures, debt service requirements, expansion strategy, or other needs;
- placing us at a competitive disadvantage compared to competitors with less debt;
- increasing our vulnerability to, and reducing our flexibility in planning for, adverse changes in economic, industry, and competitive conditions; and
- increasing our vulnerability to increases in interest rates if borrowings under the credit facility are subject to variable interest rates.

Our credit facility also contains negative covenants that limit our ability to engage in specified types of transactions. These covenants limit our ability to, among other things:

- incur indebtedness;
- create liens;
- engage in mergers or consolidations;
- sell assets (including pursuant to sale and leaseback transactions);
- pay dividends and distributions or repurchase our capital stock;
- make investments, acquisitions, loans, or advances;
- make capital expenditures;
- repay, prepay, or redeem certain indebtedness;
- engage in certain transactions with affiliates;
- enter into agreements limiting subsidiary distributions;
- enter into agreements limiting the ability to create liens;
- amend our organizational document in a way that has a material effect on the lenders or administrative agent under our credit facility; and

· change our lines of business.

A breach of any of these covenants could result in an event of default under our credit facility. Upon the occurrence of an event of default, the lender could elect to declare all amounts outstanding under such facility to be immediately due and payable and terminate all commitments to extend further credit, or seek amendments to our debt agreements that would provide for terms more favorable to such lender and that we may have to accept under the circumstances. If we were unable to repay those amounts, the lender under our credit facility could proceed against the collateral granted to them to secure that indebtedness.

If we fail to hire, train, and retain qualified managers, sales associates, and other employees, our enhanced customer service could be compromised and we could lose sales to our competitors.

A key element of our competitive strategy is to provide product expertise to our customers through our extensively trained, commissioned sales associates. If we are unable to attract and retain qualified personnel and managers as needed in the future, including qualified sales personnel, our level of customer service may decline, which may decrease our revenues and profitability.

If we are unable to renew or replace current store leases or if we are unable to enter into leases for additional stores on favorable terms, or if one or more of our current leases is terminated prior to expiration of its stated term and we cannot find suitable alternate locations, our growth and profitability could be negatively impacted.

We currently lease all of our store locations. Many of our current leases provide us with the unilateral option to renew for several additional rental periods at specific rental rates. Our ability to re-negotiate favorable terms on an expiring lease or to negotiate favorable terms for a suitable alternate location, and our ability to negotiate favorable lease terms for additional store locations, could depend on conditions in the real estate market, competition for desirable properties, our relationships with current and prospective landlords, or on other factors that are not within our control. Any or all of these factors and conditions could negatively impact our growth and profitability.

Compliance with laws or changes in existing or new laws and regulations or regulatory enforcement priorities could adversely affect our business.

We must comply with various laws and regulations at the local, regional, state, federal, and international levels. These laws and regulations change frequently and such changes can impose significant costs and other burdens of compliance on our business and vendors. Any changes in regulations, the imposition of additional regulations, or the enactment of any new legislation that affect employment/labor, trade, product safety, transportation/logistics, energy costs, health care, tax, or environmental issues, or compliance with the Foreign Corrupt Practices Act, could have an adverse impact on our financial condition and results of operations. Changes in enforcement priorities by governmental agencies charged with enforcing existing laws and regulations can increase our cost of doing business.

We may also be subject to audits by various taxing authorities. Changes in tax laws in any of the multiple jurisdictions in which we operate, or adverse outcomes from tax audits that we may be subject to in any of the jurisdictions in which we operate, could result in an unfavorable change in our effective tax rate, which could have an adverse effect on our business and results of operations.

As our stores are generally concentrated in the mid-western and mid-Atlantic regions of the United States, we are subject to regional risks.

We have a high concentration of stores in the mid-western and mid-Atlantic regions. If these markets individually or collectively suffer an economic downturn or other significant adverse event, there could be an adverse impact on same store sales, revenues, and profitability, and the ability to implement our planned expansion program. Any natural disaster or other serious disruption in these markets due to fire, tornado, hurricane, or any other calamity could damage inventory and could result in decreased revenues.

Our results may be adversely affected by fluctuations in raw material and energy costs.

Our results may be affected by the prices of the components and raw materials used in the manufacture of tile, setting and maintenance materials, and related accessories that we sell. These prices may fluctuate based on a number of factors beyond our control, including: oil prices, changes in supply and demand, general economic conditions, labor costs, competition, import duties, tariffs, currency exchange rates, and government regulation. In addition, energy costs have fluctuated dramatically in the past and may fluctuate in the future. These fluctuations may result in an increase in our transportation costs for distribution from our regional distribution centers to our retail stores, utility costs for our distribution and manufacturing centers and retail stores, and overall costs to purchase products from our vendors.

We may not be able to adjust the prices of our products, especially in the short-term, to recover these cost increases in raw materials and energy. A continual rise in raw material and energy costs could adversely affect consumer spending and demand for our products and increase our operating costs, both of which could have a material adverse effect on our financial condition and results of operations.

Our success is highly dependent on our ability to provide timely delivery to our customers, and any disruption in our delivery capabilities or our related planning and control processes may adversely affect our operating results.

Our success is due in part to our ability to deliver products quickly to our customers, which relies on successful planning and distribution infrastructure, including ordering, transportation and receipt processing, and the ability of suppliers to meet distribution requirements. Our ability to maintain this success depends on the continued identification and implementation of improvements to our planning processes, distribution infrastructure, and supply chain. We also need to ensure that our distribution infrastructure and supply chain keep pace with our anticipated growth and increased number of stores. The cost of these enhanced processes could be significant and any failure to maintain, grow, or improve them could adversely affect our operating results. Our business could also be adversely affected if there are delays in product shipments due to freight difficulties, strikes, or other difficulties at our suppliers' principal transport providers, or otherwise.

Damage, destruction, or disruption of our distribution and manufacturing centers could significantly impact our operations and impede our ability to produce and distribute our products.

We rely on three regional distribution centers to supply products to all of our retail stores. In addition, we rely on our two manufacturing centers, located at two of our distribution centers, to manufacture our setting and maintenance materials. If any of these facilities, or the inventory stored in these facilities, were damaged or destroyed by fire or other causes, our distribution or manufacturing processes would be disrupted, which could cause significant delays in delivery. This could negatively impact our ability to stock our stores and deliver products to our customers, and cause our revenues and operating results to deteriorate.

Our ability to control labor costs is limited, which may negatively affect our business.

Our ability to control labor costs is subject to numerous external factors, including prevailing wage rates, the impact of legislation or regulations governing healthcare benefits or labor relations, such as the Employee Free Choice Act, and health and other insurance costs. If our labor and/or benefit costs increase, we may not be able to hire or maintain qualified personnel to the extent necessary to execute our competitive strategy, which could adversely affect our results of operations.

Our business exposes us to personal injury and product liability claims, which could result in adverse publicity and harm to our brands and our results of operations.

We are from time to time subject to claims due to the injury of an individual in our stores or on our property. In addition, we may be subject to product liability claims for the products that we sell. Our purchase orders generally do not require the manufacturer to indemnify us against any product liability claims arising from products purchased by us. Any personal injury or product liability claim made against us, whether or not it has merit, could be time-consuming and costly to defend, resulting in adverse publicity or damage to our reputation, and have an adverse effect on our results of operations. In addition, any negative publicity involving our vendors, employees, and other parties who are not within our control could negatively impact us.

Our business operations could be disrupted if our information technology systems fail to perform adequately or we are unable to protect the integrity and security of our customers' information.

We depend upon our information technology systems in the conduct of all aspects of our operations. If our information technology systems fail to perform as anticipated, we could experience difficulties in virtually any area of

our operations, including but not limited to replenishing inventories or delivering products to store locations in response to consumer demands. It is also possible that our competitors could develop better online platforms than us, which could negatively impact our internet sales. Any of these or other systems-related problems could, in turn, adversely affect our revenues and profitability.

In addition, in the ordinary course of our business, we collect and store certain personal information from individuals, such as our customers and suppliers, and we process customer payment card and check information. We also store credit card information and other personal information about our customers and we are currently assessing our compliance laws associated with the collection, security, and handling of personal information and intend to make any required changes in our systems and policies in response to this assessment. Our failure to comply with such laws, a breach of our network security and systems, or other events that cause the loss or public disclosure of, or access by third parties to, our customers' personal information could have serious negative consequences for our business, including possible fines, penalties and damages, an unwillingness of customers to provide us with their credit card or payment information, harm to our reputation and brand, loss of our ability to accept and process customer credit card orders, and time-consuming and expensive litigation.

Computer hackers may attempt to penetrate our computer systems and, if successful, misappropriate personal information, payment card or check information, or confidential business information. In addition, an employee, contractor, or other third party with whom we do business may attempt to circumvent our security measures in order to obtain such information. The techniques used to obtain unauthorized access or sabotage systems change frequently and may originate from less regulated or remote areas around the world. As a result, we may be unable to proactively address these techniques or to implement adequate preventative measures.

Many states have enacted laws requiring companies to notify individuals of data security breaches involving their personal data. These mandatory disclosures regarding a security breach often lead to widespread negative publicity, which may cause our customers to lose confidence in the effectiveness of our data security measures. Any security breach, whether successful or not, would harm our reputation and could cause the loss of customers.

We may not be able to timely and effectively implement controls and procedures required by Section 404 of the Sarbanes-Oxley Act of 2002 that are applicable to us.

We are subject to Section 404 of the Sarbanes-Oxley Act of 2002. The standards required for us as a public company under Section 404 of the Sarbanes-Oxley Act of 2002 are significantly more stringent than those required of us as a privately-held company. Management may not be able to effectively and timely implement controls and procedures that adequately respond to the increased regulatory compliance and reporting requirements that are applicable to us. If management is not able to implement the additional requirements of Section 404 in a timely manner or with adequate compliance, management may not be able to assess whether our internal controls over financial reporting are effective, which may subject us to adverse regulatory consequences and could harm investor confidence and the market price of our securities

Concentration of ownership may have the effect of delaying or preventing a change in control.

Our directors, executive officers, and holders of more than 5% of our common stock, together with their affiliates, beneficially hold a majority of our outstanding shares of common stock. As a result, these stockholders, if acting together, have the ability to determine the outcome of corporate actions requiring stockholder approval. This concentration of ownership may have the effect of delaying or preventing a change in control and might adversely affect the market price of our securities.

Future sales of our common stock may cause the market price of our securities to drop significantly, even if our business is doing well.

In accordance with lock-up agreements executed in connection with the consummation of the Business Combination, the former direct and indirect holders of equity interests in The Tile Shop and the JWCAC founders and their affiliates will be permitted to sell an aggregate of 34,014,536 shares of our common stock that they received in the Business Combination (other than 290,697 earnout shares, the treatment of which is described below) on the earlier of (i) the first anniversary of the consummation of the Business Combination, (ii) the date on which the trading price of our common stock exceeds \$12.00 per share (as adjusted for stock splits, stock dividends, reorganizations, recapitalizations and the like) for any 20 trading days within any 30 trading day period commencing at least 150 days after the closing date of the Business Combination and (iii) the date on which we consummate a liquidation, merger, stock exchange or other similar transaction that results in all of our stockholders having the right to exchange their shares of our common stock for cash, securities, or other property. The JWCAC founders will be permitted to sell the 290,697 earnout shares if, prior to the second anniversary of the consummation of the Business Combination, (i) the trading price of our common stock exceeds \$12.00 per share (as adjusted for stock splits, stock dividends, reorganizations, recapitalizations and similar events) for any 20 trading days within any 30 trading day period commencing at least 150 days after the closing date of the Business Combination or (ii) we consummate a liquidation, merger, stock exchange, or other similar transaction that results in all of our stockholders having the right to exchange their shares of our common stock for cash, securities, or other property, the value of which equals or exceeds \$12.00 per share (as adjusted for stock splits, stock dividends, reorganizations, recapitalizations and similar events). The terms of the lock-up agreements may be amended by us and the other parties to such agreements.

In addition, the former direct and indirect holders of equity interests in The Tile Shop and the JWCAC founders hold registration rights, subject to certain limitations, with respect to our common stock that they received in the Business Combination pursuant to a registration rights agreement. The holders of a majority in interest of our common stock held by the former direct and indirect holders of equity interests in The Tile Shop will be entitled to require us, on up to four occasions, to register under the Securities Act of 1933, as amended, or the Securities Act, the shares of common stock that they received in the Business Combination. The holders of a majority in interest of our common stock held by the JWCAC founders will be entitled to require us, on up to two occasions, to register under the Securities Act the shares of common stock that they received in the Business Combination, and any shares that may be issued pursuant to the exercise of certain warrants held by them. The presence of these additional securities trading in

the public market may have an adverse effect on the market price of our common stock.

Although our common stock is currently listed on The NASDAQ Global Market, there can be no assurance that we will be able to comply with the continued listing standards.

The NASDAQ Global Market may delist our common stock from trading on its exchange for failure to meet the continued listing standards. If our common stock were delisted from The NASDAQ Global Market, we and our stockholders could face significant material adverse consequences including:

- a limited availability of market quotations for our common stock;
- a determination that our common stock is a “penny stock” would require brokers trading in our common stock to adhere to more stringent rules, possibly resulting in a reduced level of trading activity in the secondary trading market for our common stock;
- a limited amount of analyst coverage; and

- a decreased ability to issue additional securities or obtain additional financing in the future.

The market price of our securities may decline and/or be volatile.

Fluctuations in the price of our securities could contribute to the loss of all or part of your investment. Prior to the Business Combination, there had not been a public market for our securities or The Tile Shop's securities, and trading in JWCAC's securities had not been active. Since the Business Combination, our common stock has subsequently traded as high as \$16.99. An active, liquid, and orderly market for our securities may not be sustained and the trading price of our securities could be volatile and subject to wide fluctuations in response to various factors, some of which are beyond our control. Any of the factors listed below could have a material adverse effect on your investment in our securities and our securities may trade at prices significantly below the price that you paid for them. In such circumstances, the trading price of our securities may not recover and may experience a further decline.

Factors affecting the trading price of our securities may include:

- actual or anticipated fluctuations in our quarterly financial results or the quarterly financial results of companies perceived to be similar to us;
- changes in the market's expectations about our operating results;
- the effects of seasonality on our business cycle;
- success of competitive retailers;
- our operating results failing to meet the expectation of securities analysts or investors in a particular period;
- changes in financial estimates and recommendations by securities analysts concerning us, the housing market, the retail specialty tile market, or the retail market in general;

- operating and stock price performance of other companies that investors deem comparable to us;
- our ability to market new and enhanced products on a timely basis;
- changes in laws and regulations affecting our business;
- commencement of, or involvement in, litigation involving us;
- changes in our capital structure, such as future issuances of securities or the incurrence of additional debt;
- the volume of shares of our common stock available for public sale;
- any major change in our board of directors or management;
- sales of substantial amounts of common stock by our directors, executive officers, or significant stockholders or the perception that such sales could occur; and
- general economic and political conditions such as recessions, interest rates, fuel prices, international currency fluctuations, and acts of war or terrorism.

Broad market and industry factors may materially harm the market price of our securities irrespective of our operating performance. The NASDAQ Global Market and the stock market in general have experienced price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of the particular companies affected. The trading prices and valuations of these securities, and of our securities, may not be predictable. A loss of investor confidence in the market for retail securities or the securities of other companies that investors perceive to be similar to us could depress the price of our securities regardless of our business, prospects, financial conditions, or results of operations. A decline in the market price of our securities also could adversely affect our ability to issue additional securities and our ability to obtain additional financing in the future.

If securities or industry analysts do not publish or cease publishing research or reports about us, our business, or our market, or if they change their recommendations regarding our common stock adversely, the price and trading volume of our common stock could decline.

The trading market for our common stock will be influenced by the research and reports that industry or securities analysts may publish about us, our business, our market, or our competitors. If any of the analysts who cover us change their recommendation regarding our common stock adversely, or provide more favorable relative recommendations about our competitors, the price of our common stock would likely decline. If any analyst who covers us were to cease coverage of us or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our common stock price or trading volume to decline.

The exercise of warrants to purchase shares of our common stock will increase the number of shares eligible for future resale in the public market and result in dilution to our existing stockholders.

There are outstanding warrants to purchase an aggregate of 17,771,232 shares of our common stock. To the extent such warrants are exercised, additional shares of our common stock will be issued, which will result in dilution to the existing holders of our common stock and increase the number of shares eligible for resale in the public market. Sales of substantial numbers of such shares in the public market could adversely affect the market price of our common stock.

Our management will have broad discretion over the use of the proceeds that we receive from the exercise of the warrants to purchase shares of our common stock and might not apply the proceeds in ways that increase the value of our securities.

Our management will have broad discretion to use the proceeds that we receive from the exercise of warrants to purchase shares of our common stock, and you will be relying on the judgment of our management regarding the application of these proceeds. Our management might not apply these proceeds in ways that increase the value of our

securities. We intend to use these proceeds primarily for general corporate purposes, including working capital, sales and marketing activities, general and administrative matters, repayment of indebtedness, and capital expenditures. We may also use a portion of these proceeds to acquire or invest in complementary products or businesses. Until we use these proceeds, we plan to invest them, and these investments may not yield a favorable rate of return. If we do not invest or apply the proceeds that we receive from the exercise of warrants in ways that enhance stockholder value, we may fail to achieve expected financial results, which could cause the price of our securities to decline. You will not have the opportunity to influence our decisions on how we use the proceeds that we receive from the exercise of warrants.

We may redeem certain outstanding warrants to purchase shares of our common stock prior to their exercise at a time that it is disadvantageous to the holders thereof, thereby making such warrants worthless.

We have the ability to redeem certain outstanding warrants to purchase shares of our common stock at any time prior to their expiration at a price of \$0.01 per warrant, provided that (i) the last reported sale price of our common stock equals or exceeds \$18.00 per share for any 20 trading days within the 30 trading-day period ending on the third business day before we send the notice of such redemption and (ii) on the date that we give notice of redemption and during the entire period thereafter until the time all such warrants are redeemed, there is an effective registration statement under the Securities Act covering the shares of our common stock issuable upon exercise of such warrants and a current prospectus relating to them is available. Redemption of such warrants could force the holders thereof:

- to exercise their warrants and pay the exercise price therefor at a time when it may be disadvantageous for them to do so;
- to sell their warrants at the then-current market price when they might otherwise wish to hold their warrants; or
- to accept the nominal redemption price which, at the time the outstanding warrants are called for redemption, is likely to be substantially less than the market value of their warrants.

Registration of the shares of common stock underlying outstanding warrants and a current prospectus may not be in place when an investor desires to exercise warrants, thus precluding such investor from being able to exercise its warrants and causing such warrants to expire worthless.

Under the agreement governing certain of our outstanding warrants to purchase shares of our common stock, we are obligated to use our best efforts to maintain the effectiveness of a registration statement under the Securities Act for the shares of common stock issuable exercise of such warrants, and a current prospectus relating thereto, until the expiration of the warrants in accordance with the provisions of the warrant agreement. In addition, we are obligated to use our best efforts to register the shares of common stock issuable upon exercise of a warrant under the blue sky laws of the states of residence of the exercising warrant holder to the extent an exemption is not available.

In connection with the Business Combination, we registered the shares of common stock issuable upon exercise of such warrants on our registration statement on Form S-4 and intend to continue the effectiveness of such registration statement by filing any necessary post-effective amendments thereto. Nevertheless, if such registration statement is not effective on the 60th business day following the closing of the Business Combination or afterward, we will be required to permit holders to exercise their warrants on a cashless basis, under certain circumstances specified in the warrant agreement. However, no warrant will be exercisable for cash or on a cashless basis, and we will not be obligated to issue any shares to holders seeking to exercise their warrants, unless the shares issuable upon such exercise are registered or qualified under the Securities Act and securities laws of the state of the exercising holder to the extent an exemption is unavailable. In no event will we be required to issue cash, securities, or other compensation

in exchange for the warrants in the event that the shares underlying such warrants are not registered or qualified under the Securities Act or applicable state securities laws. If the issuance of the shares upon exercise of the warrants is not so registered or qualified, the holder of such warrant shall not be entitled to exercise such warrant and such warrant may have no value and expire worthless. If and when the warrants become redeemable, we may exercise our redemption right even if we are unable to register or qualify the underlying shares of common stock for sale under all applicable state securities laws.

We are a holding company with no business operations of our own and depend on cash flow from The Tile Shop to meet our obligations.

We are a holding company with no business operations of our own or material assets other than the equity of our subsidiaries. All of our operations are conducted by our subsidiary, The Tile Shop. As a holding company, we will require dividends and other payments from our subsidiaries to meet cash requirements. The terms of any credit facility may restrict our subsidiaries from paying dividends and otherwise transferring cash or other assets to us. If there is an insolvency, liquidation, or other reorganization of any of our subsidiaries, our stockholders likely will have no right to proceed against their assets. Creditors of those subsidiaries will be entitled to payment in full from the sale or other disposal of the assets of those subsidiaries before us, as an equityholder, would be entitled to receive any distribution from that sale or disposal. If The Tile Shop is unable to pay dividends or make other payments to us when needed, we will be unable to satisfy our obligations.

Anti-takeover provisions contained in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could impair a takeover attempt.

Our certificate of incorporation and bylaws contain provisions that could have the effect of delaying or preventing changes in control or changes in our management without the consent of our board of directors. These provisions include:

- a classified board of directors with three-year staggered terms, which may delay the ability of stockholders to change the membership of a majority of our board of directors;
- no cumulative voting in the election of directors, which limits the ability of minority stockholders to elect director candidates;
- the exclusive right of our board of directors to elect a director to fill a vacancy created by the expansion of the board of directors or the resignation, death, or removal of a director, which prevents stockholders from being able to fill vacancies on our board of directors;
- the ability of our board of directors to determine to issue shares of preferred stock and to determine the price and other terms of those shares, including preferences and voting rights, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;
- a prohibition on stockholder action by written consent, which forces stockholder action to be taken at an annual or special meeting of our stockholders;
- the requirement that a special meeting of stockholders may be called only by the chairman of the board of directors, the chief executive officer, or the board of directors, which may delay the ability of our stockholders to force consideration of a proposal or to take action, including the removal of directors;
- limiting the liability of, and providing indemnification to, our directors and officers;

- controlling the procedures for the conduct and scheduling of stockholder meetings;
- providing the board of directors with the express power to postpone previously scheduled annual meetings of stockholders and to cancel previously scheduled special meetings of stockholders;
- providing that directors may be removed prior to the expiration of their terms by stockholders only for cause; and
- advance notice procedures that stockholders must comply with in order to nominate candidates to our board of directors or to propose matters to be acted upon at a stockholders' meeting, which may discourage or deter a potential acquiror from conducting a solicitation of proxies to elect the acquiror's own slate of directors or otherwise attempting to obtain control of us.

These provisions, alone or together, could delay hostile takeovers and changes in control of us or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation Law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock. Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

USE OF PROCEEDS

We will receive the proceeds from the exercise of the Public Warrants, but not from the sale of the underlying shares of common stock. We intend to use the proceeds from the exercise of the Public Warrants primarily for general corporate purposes, including working capital, sales and marketing activities, general and administrative matters, repayment of indebtedness, and capital expenditures. We may also use a portion of the proceeds to acquire or invest in complementary products or businesses. Our management will have broad discretion over the uses of the proceeds from the exercise of the Public Warrants. Pending these uses, we intend to invest the net proceeds from the exercise of Public Warrants in short-term, investment-grade, interest-bearing securities such as money market accounts, certificates of deposit, commercial paper, and guaranteed obligations of the U.S. government.

PLAN OF DISTRIBUTION

The shares of common stock offered and sold pursuant to this prospectus will be issued directly to the holders of Public Warrants upon payment of the exercise price therefore to us. We are required to pay all fees and expenses incident to the registration of the shares of our common stock to be offered and sold pursuant to this prospectus.

PRICE RANGE OF SECURITIES

Our common stock has been traded on The NASDAQ Global Market under the symbol “TTS” since the consummation of the Business Combination on August 21, 2012. Prior to this time, there was no public market for our common stock. Our Public Warrants are quoted on the Over-the-Counter Bulletin Board under the symbol “TTSAW.” The following table shows the high and low sale prices per share of our common stock and Public Warrants as reported on The NASDAQ Global Market and the Over-the-Counter Bulletin Board for the periods indicated:

	Common Stock		Public Warrants	
	High	Low	High	Low
Third Quarter 2012 (beginning August 21, 2012)	\$ 16.99	\$ 11.75	\$ 3.60	\$ 1.10
Fourth Quarter 2012 (through November 12, 2012)	\$ 15.26	\$ 12.00	\$ 3.94	\$ 2.95

On November 12, 2012, the closing prices of our common stock and Public Warrants were \$13.69 and \$3.27, respectively. As of November 12, 2012 we had approximately 34 holders of record of our common stock and 15 holders of record of our Public Warrants. These figures do not include the number of persons whose securities are held

in nominee or “street” name accounts through brokers.

DIVIDENDS

We have never declared or paid, and do not anticipate declaring or paying, any cash dividends on our common stock in the foreseeable future. While our board of directors may consider whether or not to institute a dividend policy, it is our present intention to retain any earnings for use in our business operations.

CAPITALIZATION

The following table sets forth our cash and cash equivalents and capitalization as of September 30, 2012. This table should be read in conjunction with the information provided in “Selected Consolidated Financial Data,” “Management's Discussion and Analysis of Financial Condition and Results of Operations” and our consolidated financial statements and related notes.

	As of September 30, 2012 (in thousands)
Cash and cash equivalents	\$ 5,961
Long-term liabilities:	
Long-term debt, net of current portion	1,085
Deferred rent	17,751
Capital lease obligations, net of current portion	1,479
Promissory notes	66,271
Total long-term liabilities	86,586
Stockholders' equity:	
Common stock, par value \$0.0001 per share; authorized: 100,000,000 shares; issued: 42,891,985 shares	4
Preferred stock, par value \$0.0001 per share; authorized: 10,000,000 shares; issued: 0 shares	-
Additional paid-in-capital	18,984
Retained earnings	23,318
Total stockholders' equity	42,306
Total capitalization	\$ 128,892

The outstanding share information set forth above is as of September 30, 2012 and excludes:

- 450,000 shares of common stock, subject to increase on an annual basis, reserved for issuance under our 2012 Equity Award Plan;
- 1,755,000 shares of common stock issuable upon exercise of outstanding options to purchase shares of common stock granted pursuant to our 2012 Equity Award Plan; and

- 17,771,232 shares of common stock issuable upon exercise of outstanding warrants to purchase shares of common stock at an exercise price of \$11.50 per share.

SUMMARY CONSOLIDATED FINANCIAL AND OTHER DATA

The following table sets forth selected historical financial information derived from (i) our unaudited financial statements included elsewhere in this prospectus as of and for the nine months ended September 30, 2012 and 2011, (ii) The Tile Shop's audited financial statements included elsewhere in this prospectus as of December 31, 2011 and 2010 and for the years ended December 31, 2011, 2010 and 2009 and (iii) The Tile Shop's audited financial statements not included in this report as of December 31, 2009, 2008 and 2007 and for the years ended December 31, 2008 and 2007. You should read the following selected financial data in conjunction with the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the financial statements and the related notes appearing elsewhere in this prospectus.

	As of September 30, or for the nine months ended September 30,			As of December 31, or for the year ended December 31,			
	2012	2011	2011	2010	2009	2008	2007
Statement of Income Data							
Net sales	\$ 136,463	\$ 115,015	\$ 152,717	\$ 135,340	\$ 116,247	\$ 118,960	\$ 111,607
Cost of sales	37,025	30,298	40,321	36,124	31,706	34,001	33,588
Gross profit	99,438	84,717	112,396	99,216	84,541	84,959	78,019
Selling, general and administrative expenses	68,606	58,225	78,368	68,105	60,051	61,322	58,539
Deferred compensation expense	3,897	966	1,415	450	120	260	150
Income from operations	26,935	25,526	32,613	30,661	24,370	23,377	19,330
Interest expense	626	297	443	467	545	592	972
Other income (expense)	23	36	(77)	(810)	(1,017)	(509)	(1,381)
Income before income taxes	26,332	25,265	32,093	30,318	23,898	23,460	18,921
Benefit (provision) for income taxes ⁽¹⁾	4,299	(578)	(733)	(609)	(675)	(724)	(461)
Net income	\$ 30,631	\$ 24,687	\$ 31,360	\$ 29,709	\$ 23,223	\$ 22,736	\$ 18,460
Earnings per share ⁽¹⁾	\$ 0.91	\$ 0.77	\$ 0.97	\$ 0.92	\$ 0.72	\$ 0.70	\$ 0.57
Weighted average share outstanding	33,544	32,000	32,261	32,330	32,330	32,330	32,330

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Balance Sheet
Data

Cash and cash equivalents	\$ 5,960	\$ 12,253	\$ 6,283	\$ 14,117	\$ 17,850	\$ 3,631	\$ 638
Inventories	40,662	42,704	43,744	35,358	26,342	28,046	22,891
Total assets	161,830	122,512	119,005	108,890	95,632	80,225	78,802
Total debt and capital lease obligations, including current maturities	73,226	4,964	4,853	5,582	4,574	5,035	6,334
Total stockholders' equity	42,306	81,492	75,147	69,437	62,000	49,586	39,084
Working capital	28,880	42,347	34,852	34,895	31,851	18,949	9,980

Cash Flow
Data

Net cash provided by operating activities	\$ 41,540	\$ 23,597	\$ 34,723	\$ 32,461	\$ 34,729	\$ 25,156	\$ 27,885
Net cash used in investing activities	(17,187)	(11,372)	(18,561)	(14,376)	(8,267)	(9,435)	(12,928)
Net cash used in financing activities	(24,676)	(14,089)	(23,994)	(21,819)	(12,243)	(12,728)	(14,330)

Other Selected
Financial Data
(unaudited)

Adjusted EBITDA ⁽²⁾	\$ 38,662	\$ 32,687	\$ 42,602	\$ 38,472	\$ 31,576	\$ 30,818	\$ 25,832
Adjusted EBITDA margin ⁽²⁾	28.3 %	28.4 %	27.9 %	28.4 %	27.2 %	25.9 %	23.1 %
Gross margin ⁽³⁾	72.9 %	73.7 %	73.6 %	73.3 %	72.7 %	71.4 %	69.9 %
Operating income margin ⁽⁴⁾	19.7 %	22.2 %	21.4 %	22.7 %	21.0 %	19.7 %	17.3 %
Same stores sales growth ⁽⁵⁾	5.5 %	6.1 %	6.4 %	11.4 %	(4.6)%	(3.4)%	3.4 %

(1) Historical results do not include pro forma adjustments for income taxes as a result of The Tile Shop's change in tax status, which was effective on August 21, 2012.

(2) We calculate Adjusted EBITDA by taking net income calculated in accordance with accounting principles generally accepted in the United States, or GAAP, and adding interest expense, income taxes, depreciation and amortization, deferred compensation, and stock-based compensation. Adjusted EBITDA margin is equal to Adjusted EBITDA divided by net sales. 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 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.

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 limitation of these non-GAAP financial measures is that they exclude significant expenses and income that are required by GAAP to be recorded 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.

	Nine Months Ended		Years Ended December 31,				
	September 30,						
	2012	2011	2011	2010	2009	2008	2007
Net Income	\$ 30,631	\$ 24,687	\$ 31,360	\$ 29,709	\$ 23,223	\$ 22,736	\$ 18,460
Interest expense	626	297	443	467	545	592	972
Income taxes	(4,299)	579	733	609	675	724	461
Depreciation and amortization	7,543	6,158	8,651	7,237	7,013	6,506	5,789
Deferred compensation expense	3,898	966	1,415	450	120	260	150
Stock-based compensation	263	-	—	—	—	—	—
Adjusted EBITDA	\$ 38,662	\$ 32,687	\$ 40,602	\$ 38,472	\$ 31,576	\$ 30,818	\$ 25,832

(3) Gross margin is gross profit divided by net sales.

(4) Operating income margin is income from operations divided by net sales.

(5) Same store sales growth is the percentage change in sales of comparable stores period over period. A store is considered comparable on the first day of the 13th month of operation. Same store sales growth amounts include total charges to customers less any actual returns. We do not include estimated return provisions or sale allowances in the same store sales calculation, as return reserves are calculated on a consolidated level, and the analysis does not include website sales. Same store sales data reported by other companies may be prepared on a different basis and therefore may not be useful for purposes of comparing our results to those of other businesses.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis together with "Selected Historical Consolidated Financial Data" and our consolidated financial statements and related notes included elsewhere in prospectus. Among other things, those historical consolidated financial statements include more detailed information regarding the basis of presentation for the financial data than are included in the following discussion. This discussion contains forward-looking statements about our business, operations, and industry that involve risks and uncertainties, such as statements regarding our plans, objectives, expectations, and intentions. Our future results and financial condition may differ materially from those that we currently anticipate as a result of the factors described in the sections entitled "Risk Factors" and "Information Concerning Forward-Looking Statements."

Overview

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. We operate 62 stores in 20 states, with an average size of 23,000 square feet. We also sell our products on our website.

We purchase our tile products and accessories directly from producers and manufacture our own setting and maintenance materials, such as thinset, grout, and sealers. We believe that our long-term producer 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, 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 stone tiles, accessories, and related materials in the United States.

We believe that the highly-fragmented U.S. retail tile market provides us with a significant opportunity to expand our store base. We have opened nine new stores in the U.S. in 2012, and plan to open an additional four stores during the remainder of 2012 and no fewer than 15 stores in 2013. 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.

In 2011, we reported net sales and income from operations of \$152.7 million and \$32.6 million, respectively. From December 31, 2007 to December 31, 2011, our net sales and income from operations increased at compounded annual growth rates of 8.2% and 14.0%, respectively. During that period, we opened 14 new retail locations and focused on

cost control and implementing selected price increases in order to maintain our gross profit and income from operations. We plan to continue to focus on store growth and controlling costs.

Net cash flows provided by operating activities were \$34.7 million and \$32.5 million for 2011 and 2010, respectively, which were used to fund capital expenditures for opening new stores and daily operations. We expect to continue to fund our capital expenditures and daily operations from our operating cash flows and with borrowings pursuant to our credit facility. As of September 30, 2012, we had cash of \$6.0 million and working capital of \$28.9 million.

We plan to continue to invest in strong customer service by leveraging our highly-trained staff from our existing store base to train new store staff. In 2011, we began to deploy iPOS, a hand-held mobile device that provides our sales associates with real-time access to warehouse inventory, the ability to create a new customer order, process payments, edit orders, and look up a customer's contact information and order history while on the store floor. We completed the deployment of iPOS to all of our stores in 2012. We continue to invest in our marketing and brand management, website improvements, and growing use of social media. We also plan to maintain our marketing and brand management by periodically remodeling our in-store displays and developing content about our store and products for smart phones and tablets. In 2011, approximately 50% of our net sales were from repeat customers.

As a result of the Business Combination, we anticipate incurring incremental general and administrative expenses of approximately \$2 million annually that are attributable to operating as a publicly traded company. These expenses will include annual and quarterly reporting; Sarbanes-Oxley compliance expenses; expenses associated with listing on The NASDAQ Global Market; chief financial officer and additional staff compensation; legal fees; independent auditor fees; investor relations expenses; registrar and transfer agent fees; director and officer liability insurance costs; and director compensation. In addition, we expect to incur approximately \$1.9 million annually of non-cash, stock based compensation expense. The effect of these incremental general and administrative expenses are not reflected in The Tile Shop's historical consolidated financial statements.

Our business is subject to seasonal fluctuations and generally has experienced more sales and a greater portion of income from operations during the first two quarters of our fiscal year and slower activity in the fourth quarter due to holidays. We expect this trend to continue for the foreseeable future.

Recent Developments

On October 3, 2012, we and our subsidiaries entered into a credit agreement with Bank of America, N.A. and The Huntington National Bank. The credit agreement provides us with a \$100 million senior secured credit facility, comprised of a five-year \$25 million term loan and a \$75 million revolving line of credit. 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 ranges from LIBOR plus 1.75% to 2.25%, depending on The Tile Shop's leverage ratio. Borrowings under the term loan require quarterly principal payments of \$0.875 million. The base rate will be equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Bank of America "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.75% to 1.25% depending on The Tile Shop's leverage ratio. 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 certain types of related party transactions. The credit agreement also includes financial and other covenants including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios. In connection with the credit agreement, we and our subsidiaries also (i) entered into a security agreement pursuant to which we and each of our subsidiaries granted to the lenders under the credit agreement a first priority security interest in certain accounts, inventory, equipment, general intangibles, chattel paper, letters of credit, and other assets to secure our obligations and those of our subsidiaries under the credit agreement and (ii) agreed to guaranty the our obligations and those of subsidiaries under the credit agreement.

We have used borrowings pursuant to the credit agreement to pay all outstanding obligations pursuant to the approximately \$70 million of promissory notes that we issued in connection with the Business Combination. Additional borrowings pursuant to the credit agreement may be used to support our growth and for working capital purposes.

Key Components of our Consolidated Statements of Income

Net sales

Net sales represent total charges to customers and include freight charged to customers. The increase in net sales in recent years has been a result of store base growth, increases in same store sales, expansion of product lines, and a gradually improving national economy. From 2009 to 2011, our net sales grew 31.4% to \$152.7 million.

The table below sets forth information about our same store sales growth from 2009 to September 30, 2012. Our increase in same store sales growth is primarily attributable to increases in volume. Same store sale amounts include total charges to customers less any actual returns. We do not include estimated return provisions or sales allowances in the same store sales calculation, as return reserves are calculated at the consolidated level. In general, we consider a store comparable on the first day of the 13th month of operation.

	Nine Months Ended September 30,		Years Ended December 31,		
	2012	2011	2011	2010	2009
Same store sales growth	5.5 %	6.1 %	6.4 %	11.4 %	(4.6)%

We opened five, five, and one new stores in 2011, 2010, and 2009, respectively. Net sales at new stores are generally lowest in the first few months after a location is opened and generally increase over time. We expect a store's net sales to increase faster during its first three years of operation than in its later years. Store locations opened in existing markets tend to have higher net sales in the first year of operation than store locations opened in new markets, as a portion of such net sales come from more mature stores in those markets.

Cost of sales

Cost of sales (excluding depreciation and amortization) consists primarily of costs associated with purchasing products and delivering them to customers, as well as costs associated with manufacturing of maintenance materials.

Gross profit

Gross profit is net sales less cost of sales. Gross margin is the percentage determined by dividing gross profit by net sales.

In 2011, 2010, and 2009 our gross margin was 73.6%, 73.3%, and 72.7%, respectively. For the nine months ended September 30, 2012 and 2011 our gross margin was 72.9% and 73.7%, respectively. We have been able to maintain stable gross margins as a result of product cost control and expect that our gross margin will continue in the same range.

Selling, general, and administrative expenses

Payroll costs and occupancy expenses have historically been our most significant selling, general, and administrative expenses. Payroll costs exclude costs associated with manufacturing labor costs, as those costs are included in cost of sales. In 2011, 2010, and 2009, our selling, general, and administrative expenses as a percentage of net sales was 52.2%, 50.7%, and 51.8%, respectively. For the nine months ended September 30, 2012 and 2011, selling, general, and administrative expenses as a percentage of net sales was 50.3% and 50.6%, respectively. We expect to continue making investments in our corporate infrastructure commensurate with our growth strategy.

Since the consummation of the Business Combination, we have incurred, and expect to continue to incur, increased incremental general and administrative expenses attributable to operating as a publicly traded company. These costs include those associated with Securities and Exchange Commission reporting, Sarbanes-Oxley compliance, and listing on The NASDAQ Global Market, as well as increased compensation to our financial personnel, professional fees, insurance costs, director compensation.

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 rates for the three and nine months ended September 30, 2012 are not necessarily indicative of the effective tax rate that may be expected for fiscal year 2012 or future periods.

Adjusted EBITDA

We calculate Adjusted EBITDA by taking net income calculated in accordance with accounting principles generally accepted in the United States, or GAAP, and adding interest expense, income taxes, depreciation and amortization, deferred compensation, and stock-based compensation. Adjusted EBITDA margin is equal to Adjusted EBITDA divided by net sales. 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 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.

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 limitation of these non-GAAP financial measures is that they exclude significant expenses and income that are required by GAAP to be recorded 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.

	Nine Months Ended		Years Ended December 31,				
	September 30,		2011	2010	2009	2008	2007
	2012	2011	2011	2010	2009	2008	2007
Net income	\$ 30,631	\$ 24,687	\$ 31,360	\$ 29,709	\$ 23,223	\$ 22,736	\$ 18,460
Interest expense	626	297	443	467	545	592	972
Income taxes	(4,299)	579	733	609	675	724	461
Depreciation and amortization	7,543	6,158	8,651	7,237	7,013	6,506	5,789
Deferred compensation expense	3,898	966	1,415	450	120	260	150
Stock-based compensation	263	-	—	—	—	—	—
Adjusted EBITDA	\$ 38,662	\$ 32,687	\$ 42,602	\$ 38,472	\$ 31,576	\$ 30,818	\$ 25,832

Comparison of the Nine Months Ended September 30, 2012 and the Nine Months Ended September 30, 2011

	Nine months ended September 30			
	2012	% of sales	2011	% of sales
Net sales	\$ 136,463,028		\$ 115,014,677	
Cost of sales	37,025,108	27.1 %	30,297,496	26.3 %
Gross profit	99,437,920	72.9 %	84,717,181	73.7 %
Selling, general and administrative expenses	68,605,613	50.3 %	58,224,776	50.6 %
Deferred compensation expense	3,896,799	2.9 %	966,439	0.8 %
Income from operations	26,935,508	19.7 %	25,525,966	22.2 %
Interest expense	626,023	0.5 %	296,839	0.3 %
Other income (expense)	23,052	0.0 %	36,116	0.0 %
Income before income taxes	26,332,537	19.3 %	25,265,243	22.0 %
Benefit (provision) for income taxes	4,298,866	3.2 %	(578,603)	-0.5 %
Net income	\$ 30,631,403	22.4 %	\$ 24,686,640	21.5 %

Net sales

Net sales increased by \$21.4 million, or 18.6%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011. This increase is primarily due to net sales of \$14.8 million from 11 new stores, and an increase of \$6.6 million from same store sales growth.

Gross profit

Gross profit increased \$14.7 million, or 17.4%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011, primarily due to the increase in net sales. Gross margin decreased 0.9% for the nine months ended September 30, 2012 from the nine months ended September 30, 2011, primarily due to slightly higher product related costs and transportation expenses.

Selling, general, and administrative expenses

Selling, general, and administrative expenses increased \$10.4 million, or 17.8%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011. Selling, general, and administrative expenses as a percentage of net sales decreased from 50.6% to 50.3% for the nine months ended September 30, 2012 compared to nine months ended September 30, 2011. The increase in selling, general, and administrative expenses was primarily due to increased payroll costs of \$5.5 million, increased rent and occupancy costs of \$1.5 million, and increased depreciation and amortization of \$1.4 million, primarily as a result of opening new stores. Selling, general and administrative expense also included an increase in stock compensation expense of \$0.3 million.

Deferred compensation expense

Deferred compensation expenses increased \$2.9 million, or 303%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011. The increase in deferred compensation expense was primarily due to the termination of The Tile Shop's historical equity incentive deferred compensation plan, or the Deferred Compensation Plan, and the related agreement to make a lump-sum cash payment to each former participant in our Deferred Compensation Plan, as well as accelerated vesting of certain membership interests in The Tile Shop in connection with the consummation of the Business Combination. We will not recognize any additional expense related to the foregoing.

Income from operations and operating margin

As a result of the above, income from operations increased by \$1.4 million, or 5.5%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011. Operating income margin decreased from 22.2% to 19.7% for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011. Excluding the non-recurring deferred compensation costs in each period, income from operations would have been \$30.8 million and \$26.5 million for the nine months ended September 30, 2012 and 2011, respectively, which represents a 16.2% increase in the 2012 period from the 2011 period.

Interest expense

Interest expense increased \$0.3 million, or 111%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011. The increase is primarily due to interest incurred on the promissory notes issued in connection with the Business Combination, which have been repaid in full. In future periods, we expect interest expense to be consistent with or slightly higher than the expense for the three months ended September 30, 2012 as a result of borrowings under our credit facility.

Income tax provision (benefit)

Income tax benefit increase \$4.8 million for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011 as a result of our becoming a taxable entity rather than a pass-through entity. In connection with becoming a taxable entity as a result of the Business Combination, we recognized \$5.3 million of net deferred tax assets, which was offset by a tax expense of \$0.5 million for the period from August 21, 2012 through September 30, 2012.

Net income

As a result of the above, net income increased by \$5.9 million, or 24.1%, for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011.

Comparison of 2011 to 2010

	Years Ended December 31,			
	2011	% of sales	2010	% of sales
Net sales	\$ 152,717		\$ 135,340	
Cost of sales	40,321	26.4 %	36,124	26.7 %
Gross profit	112,396	73.6 %	99,216	73.3 %
Selling, general and administrative expenses	78,368	51.3 %	68,105	50.3 %
Deferred compensation expense	1,415	0.9 %	450	0.3 %
Income from operations	32,613	21.4 %	30,661	22.7 %
Interest expense	443	0.3 %	467	0.3 %
Other income (expense)	(77)	(0.1)%	124	0.1 %
Income before income taxes	32,093	21.0 %	30,318	22.4 %
Benefit (provision) for income taxes	(733)	(0.5)%	(609)	(0.4)%
Net income	\$ 31,360	20.5 %	\$ 29,709	22.0 %

Net sales

Net sales increased by \$17.4 million, or 12.8%, from 2010 to 2011. This increase is primarily due to a net sales increase of \$2.6 million from five new stores, an increase of \$14.4 million from same store sales growth, and an increase of \$0.4 million from online store sales. In 2011, we also expanded the number of products that we sell.

Gross profit

Gross profit increased \$13.2 million, or 13.3%, from 2010 to 2011, primarily due to the increase in net sales. Gross margin increased from 73.3% to 73.6% from 2010 to 2011.

Selling, general, and administrative expenses

Selling, general, and administrative expenses increased \$11.2 million, or 16.4%, from 2010 to 2011. Selling, general, and administrative expenses as a percentage of net sales increased 1.5% from 2010 to 2011. The increase in selling, general, and administrative expenses was primarily due to increased payroll costs of \$5.5 million and additional occupancy costs of \$3.4 million, primarily as a result of opening new stores. Occupancy costs are higher for new stores compared to existing stores due to the gradually improving economy and opening new stores in more expensive real estate markets. In 2011, selling, general, and administrative expenses also includes a charge of \$1.4 million related to our Deferred Compensation Plan.

Income from operations and operating margin

As a result of the above, income from operations increased by \$2.0 million, or 6.4%, from 2010 to 2011. Operating income margin decreased from 22.7% to 21.4% from 2010 to 2011.

Net income

As a result of the changes noted above, net income increased by \$1.7 million, or 5.6%, from 2010 to 2011.

Comparison of 2010 to 2009

	Years Ended December 31,			
	2010	% of sales	2009	% of sales
Net sales	\$ 135,340		\$ 116,247	
Cost of sales	36,124	26.7 %	31,706	27.3 %
Gross profit	99,216	73.3 %	84,541	72.7 %
Selling, general and administrative expenses	68,105	50.3 %	60,051	51.7 %
Deferred compensation expense	450	0.3 %	120	0.1 %
Income from operations	30,661	22.7 %	24,370	21.0 %
Interest expense	467	0.3 %	545	0.5 %
Other income (expense)	124	0.1 %	73	0.1 %
Income before income taxes	30,318	22.4 %	23,898	20.6 %
Benefit (provision) for income taxes	(609)	(0.4)%	(675)	(0.6)%
Net income	\$ 29,709	22.0 %	\$ 23,223	20.0 %

Net sales

Net sales increased \$19.1 million or 16.4%, from 2009 to 2010. This increase is primarily due to a net sales increase of \$3.1 million from five new stores, an increase of \$15.8 million from same store sales growth, and an increase of \$0.2 million from online store sales.

Gross profit

Gross profit increased by \$14.7 million, or 17.4%, from 2009 to 2010, primarily due to the increase in net sales. Gross margin increased from 72.7% to 73.3% from 2009 to 2010, primarily due to minor reductions in product cost.

Selling, general, and administrative expenses

Selling, general, and administrative expenses increased \$8.1 million, or 13.4%, from 2009 to 2010. Selling, general, and administrative expenses as a percentage of net sales decreased 1.4% from 2009 to 2010. The increase in selling, general, and administrative expenses was primarily due to increased payroll costs of \$5.1 million and additional occupancy costs of \$1.5 million, primarily as a result of opening new stores.

Income from operations and operating margin

As a result of the above, income from operations increased by \$6.3 million, or 25.8%, from 2009 to 2010. Operating margin increased from 21.0% to 22.7% from 2009 to 2010.

Net income

As a result of the changes noted above, net income increased by \$6.5 million or, 27.9% from 2009 to 2010.

Liquidity and Capital Resources

Our principal liquidity requirements have been for working capital and capital expenditures. Our principal sources of liquidity are \$6.0 million of cash and cash equivalents at September 30, 2012, our cash flow from operations, and borrowings available under our credit facility. We expect to use this liquidity for general corporate purposes, including opening new stores, purchasing additional merchandise inventory, and maintaining our existing stores.

On October 3, 2012, we and our subsidiaries entered into a credit agreement with Bank of America, N.A. and The Huntington National Bank. The credit agreement provides us with a \$100 million senior secured credit facility, comprised of a five-year \$25 million term loan and a \$75 million revolving line of credit. 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 ranges from LIBOR plus 1.75% to 2.25%, depending on The Tile Shop's leverage ratio. The base rate will be equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Bank of America "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.75% to 1.25% depending on The Tile Shop's leverage ratio. Borrowings under the term loan require quarterly principal payments of \$0.875 million. 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 certain types of related party transactions.

We have used borrowings pursuant to the credit agreement to pay all outstanding obligations pursuant to the approximately \$70 million of promissory notes that we issued in connection with the Business Combination, or the Promissory Notes. Due to the fact that we effectively refinanced the Promissory Notes with borrowings under our credit facility, we have classified the Promissory Notes obligation as of September 30, 2012 in accordance with our payment obligations under our credit facility. Accordingly, the portion of the term loan provided by the credit facility that is required to be repaid within a year, along with the accrued interest on the Promissory Notes have been included in current liabilities on the September 30, 2012 balance sheet.

Additional borrowings pursuant to the credit facility may be used to support our growth and for working capital purposes.

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

In 2012, we expect to make capital expenditures of approximately \$26 million. In addition to general capital requirements, we intend to open 13 new stores during 2012, nine of which have been opened to date, with an expected aggregate cost of approximately \$18 million. We also plan to spend \$1.3 million to renovate our existing in-store displays and \$2.4 million to expand one of our distribution centers. We have made capital expenditures of approximately \$16.2 million during the nine months ended September 30, 2012. We intend to open no fewer than 15 stores at an expected aggregate cost of approximately \$21 million in 2013.

As a result of our becoming a public company in connection with the Business Combination, we anticipate incurring incremental general and administrative expenses of approximately \$2 million annually. These expenses will include annual and quarterly reporting; Sarbanes-Oxley compliance expenses; expenses associated with listing on The NASDAQ Global Market; chief financial officer and additional staff compensation; legal fees; independent auditor fees; investor relations expenses; registrar and transfer agent fees; director and officer liability insurance costs; and director compensation. The effect of these incremental general and administrative expenses are not reflected in our historical consolidated financial statements.

Our future capital requirements will vary based on the number of additional stores, distribution centers, and manufacturing facilities that we open, the number of stores that we choose to renovate, and the number and size of any acquisition that we chooses to make. 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.

Cash flows

The following table summarizes our cash flow data 2011, 2010, and 2009, and for the nine months ended September 30, 2012 and 2011.

	Nine Months Ended		Years Ended December 31,		
	September 30,				
	2012	2011	2011	2010	2009
	(in thousands)				
Net cash provided by operating activities	\$ 41,540	\$ 23,597	\$ 34,723	\$ 32,461	\$ 34,729

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Net cash used in investing activities	(17,187)	(11,372)	(18,561)	(14,376)	(8,267)
Net cash used in financing activities	(24,676)	(14,089)	(23,994)	(21,819)	(12,243)

Operating activities

Cash flows from operating activities are significantly influenced by net income, depreciation and amortization of property, plant and equipment, amortization of deferred rent, and changes in working capital.

In the nine months ended September 30, 2012, cash provided by operating activities was \$41.5 million, driven primarily by our net income of \$30.6 million, which was reduced by non-cash charges of \$7.7 million, including \$7.5 million of depreciation and amortization, \$0.3 million of stock-based compensation, \$2.2 million of deferred rent, and \$3.8 million of deferred compensation costs, offset by non-cash income tax benefit of \$5.3 million. In addition, these cash inflows were increased by a reduction in working capital of \$2.9 million, which included a \$0.4 million increase in trade receivables, a \$3.1 million decrease in inventories, a \$3.7 million increase in prepaid expenses and other current assets, a \$4.7 million increase in accounts payable, and a \$1.4 million decrease in accrued expenses and other liabilities.

In the nine months ended September 30, 2011, cash provided by operating activities was \$23.6 million, driven primarily by our net income of \$24.7 million, which was reduced by non-cash charges of \$8.7 million, including \$6.2 million of depreciation and amortization, \$1.0 million of deferred compensation, and \$1.5 million of deferred rent. These cash inflows were offset by an increase in working capital of \$9.7 million, which included a \$7.3 million increase in inventories, a \$2.3 million increase in prepaid expenses and other current assets, a \$1.0 million decrease in accounts payable, and a \$0.9 million increase in accrued expenses and other liabilities.

In 2011, cash provided by operating activities was \$34.7 million, driven primarily by our net income of \$31.4 million, which was reduced by non-cash charges of \$12.8 million, including \$8.7 million of depreciation and amortization, \$2.5 million of deferred rent, \$1.4 million of stock-based compensation, and a \$0.2 million loss on disposal of property, plant, and equipment. These cash inflows were offset by an increase in working capital of \$9.4 million, which included a \$0.2 million decrease in trade receivables, a \$8.4 million increase in inventories, a \$0.4 million increase in prepaid expenses and other current assets, a \$1.8 million decrease in accounts payable, and a \$1.0 million increase in accrued expenses and other liabilities.

In 2010, cash provided by operating activities was \$32.5 million, driven primarily by our net income of \$29.7 million, which was reduced by non-cash charges of \$9.3 million, including \$7.2 million of depreciation and amortization, \$1.5 million of deferred rent, \$0.1 million of accretion of special cash distribution units, \$0.1 million loss on disposal of property, plant, and equipment, and \$0.5 million of stock-based compensation. These cash inflows were offset by an increase in net working capital of \$6.6 million, which included a \$0.2 million increase in trade receivables, a \$9.0 million increase in inventories, a \$1.1 million increase in prepaid expenses and other current assets, a \$3.4 million increase in accounts payable, and a \$0.3 million increase in accrued expenses and other liabilities.

In 2009, cash provided by operating activities was \$34.7 million, driven primarily by our net income of \$23.2 million, which was reduced by non-cash charges of \$9.3 million, including \$7.0 million of depreciation and amortization, \$2.0 million of deferred rent, and \$0.1 million of stock-based compensation. In addition, these cash inflows were increased by a reduction in net working capital of \$2.2 million which included a \$0.1 million decrease in trade receivables, a \$1.7 million decrease in inventories, a \$0.3 million increase in prepaid expenses and other current assets, a \$0.5 million increase in account payable, and a \$0.2 million increase in accrued expenses and other liabilities.

Investing activities

Net cash used in investing activities was \$18.6 million, \$14.4 million, \$8.3 million, \$17.2 million, and \$11.4 million in 2011, 2010, 2009, and the nine months ended September 30, 2012 and 2011, respectively. Net cash used in investing activities in each period included capital purchases of store fixtures, equipment and leasehold improvements for stores opened or remodeled, and routine capital purchases of computer hardware and software.

Financing activities

Net cash used in financing activities was \$24.0 million, \$21.8 million, \$12.2 million, \$24.6 million and \$14.1 million in 2011, 2010, 2009, and the nine months ended September 30, 2012 and 2011, respectively. These cash uses were primarily due to distributions to members of The Tile Shop and principal payments on long-term debt. Cash used in financing activities in 2010 increased compared to 2009 due to higher distributions to members of The Tile Shop as a result of our strong performance in 2010 compared to 2009.

Off-balance sheet arrangements

As of September 30, 2012 and December 31, 2011, 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

The following table summarizes certain of our contractual obligations at December 31, 2011 and the effect such obligations are expected to have on our liquidity and cash flows in future periods:

	Payment Due by Period				
	Total	Less than 1 Year	1-3 Years	4-5 Years	5+ Years
	(in thousands)				
Long-term debt including principal and interest (1)	\$3,088	\$ 594	\$ 1,483	\$ 197	\$ 814
Operating lease obligations (2)	215,975	12,226	25,864	25,543	152,342
Capital lease obligations (3)	3,196	467	944	622	1,163
Total contractual obligations (4)	\$222,259	\$ 13,287	\$ 28,291	\$ 26,362	\$154,319

(1) Includes total interest of \$84,000, comprised of \$35,000 of interest for the period of less than 1 year, \$33,000 of interest for the period of 1-3 years, \$7,000 of interest for the period of 4-5 years, and \$9,000 of interest for the period of 5+ years.

(2) Includes that base or current renewal period for our operating leases, which contain varying renewal provisions.

(3) Includes total interest of \$1,347,000, comprised of \$273,000 of interest for the period of less than 1 year, \$434,000 of interest for the period of 1-3 years, \$275,000 of interest for the period of 4-5 years, and \$365,000 of interest for the period of 5+ years.

Critical Accounting Policies and Estimates

Our financial statements are prepared in accordance with GAAP. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions, and judgments that affect the reported amount of assets, liabilities, revenues, costs and expenses, and related disclosures. We base our estimates and assumptions on historical experience and other factors that we believe to be reasonable under the circumstances, but all such estimates and assumptions are inherently uncertain and unpredictable. We evaluate our estimates and assumptions on an ongoing basis. Actual results may differ from those estimates and assumptions, and it is possible that other professionals, applying their own judgment to the same facts and circumstances, could develop and support alternative estimates and assumptions that would result in material changes to our operating results and financial condition. Our most critical accounting policies are summarized below. For further information on our critical and other significant accounting policies, see the notes to the condensed consolidated financial statements appearing elsewhere in this prospectus.

Recognition of revenue

We recognize sales at the time that the customer takes possession of the merchandise. 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. Sales and other taxes are recorded net in the consolidated balance sheets but excluded from the consolidated statements of income. Net sales are reduced by an allowance for anticipated sales returns that we estimate based on historical sales trends and experience. Any reasonably likely changes that may occur in the assumptions underlying our allowance estimates would not be expected to have a material impact on our financial condition or operating performance.

Our revenue recognition accounting methodology contains uncertainties because it requires management to make assumptions and to apply judgment to estimate future sales returns and exchanges and the associated costs. The customer may receive a refund or exchange the original product for a replacement of equal or similar quality for an indefinite period of time after the original purchase. Products received back under this policy are reconditioned pursuant to state laws and resold.

We have historically not had any material changes to the estimated liability for sales returns and exchanges. However, if actual results are not consistent with its estimates or assumptions, we may be exposed to losses or gains that could be material.

Stock-based compensation

We have granted equity-linked incentives to certain of our employees. We account for equity-linked incentives in accordance with ASC 718 “*Stock Compensation*”. ASC 718 addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for equity instruments of the enterprise or liabilities that are based on the fair value of the enterprise’s equity instruments or that may be settled by the issuance of such equity instruments.

We have granted cash-settled and equity-settled awards. Prior to the consummation of the Business Combination, the cash-settled awards were classified as liabilities as required under ASC 718. At each reporting date, the liability was measured at intrinsic value with resulting changes recognized in our consolidated statements of income.

As of the consummation of Business Combination, we have only equity-settled awards. We measure compensation cost for equity-settled awards at fair value on the date of grant and recognize compensation cost in our condensed consolidated statements of income over the service or performance period through which the award is expected to vest. We determine compensation cost by using option pricing models.

Property, plant, and equipment

Property, plant and equipment is carried at cost less accumulated depreciation, which is amortized over the useful life of the assets. Leasehold improvements are amortized over the shorter of their estimated useful lives or lease period (including expected renewal periods). Property, plant, and equipment are evaluated for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Our investment in store leasehold improvements, including fixtures and equipment, is the most significant component of property, plant, and equipment.

When evaluating property, plant, and equipment for potential impairment, if certain impairment indicators exist, we first compare the carrying value of the asset's undiscounted estimated future cash flows. If the estimated future cash flows are less than the carrying value of the asset, we calculate an impairment loss. The impairment loss calculation compares the carrying value of the asset to the asset's estimated fair value, which is based on estimated future discounted cash flows. We recognize impairment if the amount of the asset's carrying value exceeds the asset's estimated fair value. Based upon the impairment review, there were no impairment losses to report in the financial statements.

Our impairment loss calculations contain uncertainties because they require management to make assumptions and to apply judgment to estimated future cash flows and asset fair values, including forecasting useful lives of the assets and selecting the discount rate that reflects the risk inherent in future cash flows.

We have not made any material changes in the policy that we use to assess impairment losses.

We have not incurred any material impairment losses in the past and do not believe that a reasonable likelihood exists that there will be a material change in the estimates or assumptions used to calculate property, plant, and equipment asset impairment losses. However, if actual results are not consistent with our estimates and assumptions used in estimating future cash flows and asset fair values, we may be exposed to losses that could be material.

New Accounting Pronouncements

There have been no new accounting pronouncements that we would expect to have a significant impact on our results of operations, financial condition or liquidity.

Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risks in the ordinary course of our business. These risks include primarily inflation, interest rate risk, and credit concentration risk.

Inflation

Inflationary factors such as increases in the cost of our products and overhead costs may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial position or results of operations to date, a high rate of inflation in the future may have an adverse effect on our ability to maintain current levels of gross margin and selling, general, and administrative expenses as a percentage of revenues if the selling prices of our products do not increase with these increased costs.

Interest rate risk

We are exposed to interest rate risk through the investment of our cash and cash equivalents and in connection with borrowings under our \$100 million credit facility. Borrowings under our revolving credit facility bear interest at either a base rate or a LIBOR-based rate, at our option. The LIBOR-based rate ranges from LIBOR plus 1.75% to 2.25%, depending on The Tile Shop's leverage ratio. The base rate will be equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Bank of America "prime rate," and (c) the Eurodollar rate plus 1.00%, in each case plus 0.75% to 1.25% depending on The Tile Shop's leverage ratio. We invest in short-term investments with maturities of three months or less. Changes in interest rates affect the interest income that we earn in connection with these investments, and therefore impacts our cash flows and results of operations.

We currently do not engage in any significant interest rate hedging activity and currently have no intention to do so in the foreseeable future. However, in an effort to mitigate losses associated with interest rate risk, we may at times in the future enter into derivative financial instruments, although we have not historically done so to a significant extent.

We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Credit concentration risk

Financial instruments, which may subject us to concentration of credit risk, consist principally of cash deposits. We maintain cash balances at financial institutions with strong credit ratings. However, the amounts invested with financial institutions are generally in excess of FDIC insurance limits.

BUSINESS

Overview

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. We sell over 4,000 products from around the world, including ceramic, porcelain, glass, and stainless steel manufactured tiles and, marble, granite, quartz, sandstone, travertine, slate, and onyx natural tiles, primarily under our proprietary Rush River, Fired Earth, and Superior brand names. We purchase our tile products and accessories directly from producers and manufacture our own setting and maintenance materials, such as thinset, grout, and sealers. We operate 62 stores in 20 states, with an average size of 23,000 square feet. We also sell our products on our website.

We believe that our long-term producer 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, 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 stone tiles, accessories, and related materials in the United States.

In 2011, we reported net sales and income from operations of \$152.7 million and \$32.6 million, respectively. From December 31, 2007 to December 31, 2011, our net sales and income from operations increased at compounded annual growth rates of 8.2% and 14.0%, respectively. During that period, our growth was driven by a combination of opening 14 new retail locations and an increase in same store sales. We have opened nine new stores in 2012 and intend to open an additional four stores during the remainder of 2012 and no fewer than 15 stores in 2013.

Competitive Strengths

We believe that the following factors differentiate us from our competitors and position us to continue to grow our specialty tile business.

Inspiring Customer Experience. Our showrooms bring our products to life. Each showroom features up to 60 different mockups, or vignettes, of bathrooms, kitchens, fireplaces, foyers, and other settings that showcase our broad array of products. Each store also features over 1,400 hand-crafted display boards showing tile that we offer for sale. Our stores are spacious, well-lit, and organized by product type to make our customers' shopping experience easy.

Broad Product Assortment at Attractive Prices. We offer over 4,000 manufactured and natural tile products, setting and maintenance materials, and accessories. We are able to maintain every-day low prices by purchasing tile and accessories directly from producers and manufacturing our own setting and maintenance materials.

Customer Service and Satisfaction . Our sales personnel are highly-trained and knowledgeable about the technical and design aspects of our products. We offer weekly do-it-yourself classes in all of our showrooms. In addition, we provide one-on-one installation training, as required, to meet customer needs. We offer a liberal return policy, with no restocking fees.

Worldwide Sourcing Capabilities. We have long-standing relationships with producers of our tiles throughout the world and work with them to design products exclusively for us. We believe that these direct relationships differentiate us from our competitors, who generally purchase commodity products through distributors. We are often the largest or exclusive customer for many of our producers.

Proprietary Branding. We sell the majority of our products under our proprietary brand names, which helps us to differentiate our products from those of our competitors. We offer products across a range of price points and quality levels that allow us to target discrete market segments and to appeal to diverse groups of customers.

Centralized Distribution System. We service our retail locations from three distribution centers. Our distribution centers can cost-effectively service stores within a 700-mile radius, providing us with the ability to open new locations in markets where we believe that we have a competitive advantage or see attractive demographics.

Experienced Team . Our management team has substantial experience in the specialty tile industry and retail sales operations. Robert Rucker, our founder and chief executive officer, has over 25 years of experience in the tile industry. Both Carl Randazzo, senior vice president — retail, and Joseph Kinder, senior vice president — operations, have been with us for over 20 years. William Watts, who serves as the chairman of our board of directors, is the former chief executive officer of General Nutrition Corporation, the chairman of Mattress Firm, Inc. and a director of Brookstone, Inc.

Historically Attractive Returns on New Store Investment. Our new stores have historically begun generating operating profit within the first year of operations and we generally recoup our initial net capital investment from a new store's four-wall profitability within the first 36 months of operations. We measure four-wall profitability as store level operating profit before pre-opening costs and depreciation and amortization.

Growth Strategy

We intend to increase our net sales and profitability through a combination of new store openings and same store sales growth. In the five years ended December 31, 2011, we grew through a combination of opening 20 new retail locations and increases in same store sales. We expect to continue to gain market share. Specific elements of our strategy for continued growth include the following:

Open New Stores . We believe that the highly-fragmented U.S. retail tile market provides us with a significant opportunity to expand our store base. Since January 1, 2012, we have opened nine new stores and plan to open an additional four stores during the remainder of 2012. We intend to open no fewer than 15 new stores in 2013, primarily in our existing markets and the mid-Atlantic, southeastern, and southern New England regions of the United States. We believe that there will continue to be additional expansion opportunities in the United States and Canada. We expect our store base growth to increase operational efficiencies.

Increase Sales and Profitability of Existing Stores. We believe that our ongoing investment in new products and our enhanced training program for our sales associates, together with our associate incentive compensation structure, will result in continued same store sales growth.

Sales Model

We appeal to customers who desire high-quality products at an attractive value. We principally sell our products directly to homeowners. We also sell products to contractors, who are primarily small businesses that have been hired by homeowners to complete tile projects. We believe that due to the average cost and relative infrequency of a tile purchase, many of our customers conduct extensive research using multiple channels before making a purchase decision. Our sales strategy emphasizes customer service by providing comprehensive and convenient education tools on our website and in our stores for our customers to learn about our products and the tile installation process. Our website contains a broad range of information regarding our tile products, setting and maintenance materials, and accessories. Customers can order samples, view catalogs, or purchase products from either our stores or website. Customers can choose to have their purchases delivered or pick them up at one of our stores. We strive to make our customers' transactions easy and efficient.

Our stores are designed to emphasize our products in a visually appealing showroom format. Our typical store is approximately 23,000 square feet, with approximately 19,000 square feet devoted to the showroom and the balance being warehouse space, which is used primarily to store customer orders waiting to be picked up or delivered. Our stores are typically accessible from major roadways and have significant visibility to passing traffic. We can adapt to a range of existing buildings, whether free-standing or in shopping centers.

Unlike many of our competitors, we devote a substantial portion of our retail store space to showrooms, including samples of our over 4,000 products and up to 60 different vignettes of bathrooms, kitchens, fireplaces, foyers, and other settings that showcase our products. Our showrooms are designed to provide our customers with a better understanding of how to integrate various types of tile in order to create an attractive presentation in their homes. Each store is also equipped with a consumer training center designed to teach customers how to properly install tile.

A typical store staff consists of a manager and 6 to 15 sales and warehouse associates. Our store managers are responsible for store operations and for overseeing our customers' shopping experience. Our store associates have flexibility to meet or beat competitor pricing.

We offer financing to customers through a branded credit card provided by a third-party consumer finance company. These credit cards, which can be used only in our stores and on our website, provide customers with a 10% discount on all purchases from us. In 2011, approximately 9% of our sales were made using our branded card.

Marketing

Unlike many of our competitors, we do not rely on significant traditional advertising expenditures to drive our net sales. We establish and maintain our credibility primarily through the strength of our products, our store experience, our customer service, and the attractiveness of our pricing. Our advertising expenditures consist primarily of paid internet search.

Our website is designed to educate consumers and to generate in-store and online sales. Visitors to our website can purchase our products directly as well as search a comprehensive knowledge base of tools on tile, including frequently asked questions, installation guides, detailed product information, catalogs, and how-to videos that explain the installation process. Our website and social media efforts have also been devoted to building brand awareness, connecting with potential customers, and building relationships with satisfied customers.

Products

We offer a complete assortment of tile products, generally sourced directly from producers, including ceramic, porcelain, glass, and stainless steel manufactured tiles, and marble, granite, quartz, sandstone, travertine, slate, and onyx natural tiles. We also offer a broad range of setting and maintenance materials, such as thinset, grout and sealers, and accessories, including installation tools, shower and bath caddies, drains, and similar products. We sell most of our products under our proprietary brand names. In total, we offers over 4,000 different tile, setting and maintenance materials, and accessory products. In 2011, our net sales were 53% from stone products, 29% from ceramic products, and 18% from setting and maintenance products.

Producers

We have long-standing relationships with producers of our tiles throughout the world and work with them to design products exclusively for us. We believe that these direct relationships differentiate us from our competitors, who generally purchase commodity products through distributors. We are often the largest or exclusive customer for many of our suppliers, which we believes enables us to obtain better prices in some circumstances.

We currently purchases tile products from approximately 120 different producers. Our top 10 tile suppliers accounted for approximately 55% of our tile purchases in 2011. We believe that alternative and competitive suppliers are available for most of our products. In 2011, approximately 53% of our purchased product was sourced from Asia, 9% from North America, 8% from South America, 29% from Europe, and 1% from other locations. Over 95% of our foreign purchases are negotiated and paid for in U.S. dollars.

Distribution and Order Fulfillment

We take possession of our products in the country of origin and arrange for transportation to our distribution centers located in Wisconsin, Michigan, and Virginia. We manufacture our setting and maintenance materials at our Wisconsin and Michigan locations.

We fulfill customer orders primarily by shipping our products to our stores where customers can either pick them up or arrange for home delivery. Orders placed on our website are shipped directly to customers' homes from our distribution centers. We continue to evaluate logistics alternatives to best service our retail store base and our customers. We believe that our existing distribution facilities will continue to play an integral role in our growth strategy, and expects to establish one or more additional distribution centers in the next five years to support geographic expansion of our retail store base.

Market

According to Catalina Research, Inc., or Catalina, the ceramic tile and stone flooring markets together represent approximately 18% of the total U.S. floor coverings market, which includes carpet and area rugs, wood flooring, resilient flooring, and laminate flooring. In its June 2012 Floor Coverings Industry Quarterly Update, Catalina estimates that U.S. sales of ceramic tile and stone flooring increased by 6.0% and 0.2%, respectively, in 2011, with U.S. sales of ceramic tile and stone flooring totaling \$3.27 billion in 2011.

The residential tile and stone market is dependent upon home-related, large-ticket discretionary spending, which is influenced by a number of complex economic and demographic factors that may vary locally, regionally, and nationally. The market is impacted by, among other things, home remodeling activity, employment levels, housing turnover (including foreclosures), real estate prices, new housing starts, consumer confidence, credit availability, and the general health of consumer discretionary spending. Many of the economic indicators associated with the tile market and generally associated with consumer discretionary spending remain weak, and although we believe that signs of market stabilization are present, we expect that the tile market will remain in a weakened state throughout 2012. Nevertheless, IBISWorld's June 2012 Industry Report projects an expected annual growth rate of sales 3.1% in the tile and marble industry over the next five years to approximately \$5.9 billion in 2017, and the Joint Center for Housing Studies of Harvard University, or JCHS, predicts a 3.5% compounded annual increase in spending on homeowner improvements from 2010 through 2015. IBISWorld further projects that demand for homeowner improvements will be driven by young professionals with disposable income who are beginning to acquire homes in greater numbers and existing homeowners turning to deferred maintenance projects as disposable income increases with an improved economy. Recent projections by JCHS indicate that homeowner improvement spending for the four-quarter period ending with the fourth quarter of 2012 will be at the highest level since the four-quarter period ending with the third quarter of 2008, at roughly \$122.6 billion, representing a 5.9% increase over the four-quarter period ending with the first quarter of 2012.

Further, according to a July 2011 U.S. Floor Covering Industry Report from Catalina, specialty retailers serving the homeowner-based segment of the tile market face intense competition from large national home centers such as Home Depot and Lowe's, with home centers having increased their market share of total U.S. retail floor coverings sales from 19.6% of total sales in 2002 to 27.5% in 2007, and 32.0% in 2010. Catalina believes that this is a result of increasing price sensitivity on the part of consumers and the ability of large national home centers to take advantage of economies of scale. In addition, the number of specialty floor retail stores has decreased significantly, falling from 16,600 locations in 1997, to 14,500 in 2007, and 12,000 in 2010, according to Catalina. IBISWorld predicts that the market presence of specialty tile and marble stores will continue to shrink under difficult macroeconomic pressures. However, with underperforming firms exiting the market, we estimate that we have gained market share, primarily through new store openings and an increase in same store sales. We expect that these trends will continue, given our sustained growth in the face of a difficult national economy and competitive environment.

Competition

The retail tile market is highly-fragmented. We compete directly with large national home centers that offer a wide range of home improvement products in addition to tile, such as Home Depot and Lowe's; regional and local specialty retailers of tile, such as Tile America, World of Tile, Century Tile, and Floor and Décor; factory-direct stores, such as Dal-Tile and Florida Tile; and a large number of privately-owned, single-site stores. We also compete indirectly with companies that sell other types of floor coverings, including wood floors, carpet, and vinyl sheet. The barriers to entry into the retail tile industry are relatively low and new or existing tile retailers could enter our markets and increase the competition that we face. Many of our competitors enjoy competitive advantages over us, such as greater name recognition, longer operating histories, more varied product offerings, and greater financial, technical, and other resources.

We believe that the key competitive factors in the retail tile industry include:

- product variety;
- customer service;
- store location; and
- price.

We believe that we compete favorably with respect to each of these factors by providing a highly diverse selection of products to our customers, at an attractive value, in appealing and convenient retail store locations, with exceptional customer service and on-site instructional opportunities. Further, while some larger factory-direct competitors manufacture their own products, most of our competitors purchase their tile from domestic manufacturers or distributors when they receive an order from a customer. As a result, we believe that it takes these retailers longer than us to deliver products to customers and that their prices tend to be higher than our prices. We also believe that we offers a broader range of products and stronger in-store customer support than these competitors.

Employees

As of September 30, 2012, we had 744 employees, 738 of whom were full-time and none of whom were represented by a union. Of these employees, 584 work in our stores, 35 work in corporate, store support, infrastructure or similar

functions, and 125 work in distribution and manufacturing facilities. We believe that we have good relations with our employees.

Intellectual Property and Trademarks

We have registered and unregistered trademarks for all of our brands, including 13 registered marks and several pending trademark applications marks in the United States. We regard our intellectual property as having significant value and our brands are an important factor in the marketing of our products. Accordingly, we have taken, and continue to take, appropriate steps to protect our intellectual property.

Government Regulation

We are subject to extensive and varied federal, state and local government regulation in the jurisdictions in which we operate, including laws and regulations relating to our relationships with our employees, public health and safety, zoning, and fire codes. We operate each of our stores, offices, and distribution and manufacturing facilities in accordance with standards and procedures designed to comply with applicable laws, codes, and regulations.

Our operations and properties are also subject to federal, state and local laws and regulations relating to the use, storage, handling, generation, transportation, treatment, emission, release, discharge and disposal of hazardous materials, substances and wastes and relating to the investigation and cleanup of contaminated properties, including off-site disposal locations. We do not incur significant costs complying with environmental laws and regulations. However, we could be subject to material costs, liabilities, or claims relating to environmental compliance in the future, especially in the event of changes in existing laws and regulations or in their interpretation.

Products that we import into the United States are subject to laws and regulations imposed in conjunction with such importation, including those issued and/or enforced by U.S. Customs and Border Protection. We work closely with our suppliers to ensure compliance with the applicable laws and regulations in these areas.

Properties

We operate 62 stores located in 20 states, including nine opened since December 31, 2011. The table below sets forth the locations and square footage of our stores:

Location	Square Footage	Location	Square Footage
Wilmington, Delaware	22,180	Ellisville, Missouri	17,750
Jacksonville, Florida*	26,186	Independence, Missouri	26,682
Dunwoody, Georgia	21,885	St. Peters, Missouri	20,200
Kennesaw, Georgia	27,000	Sunset Hills, Missouri	17,500
Countryside, Illinois	18,929	Omaha, Nebraska	20,412
Deerfield, Illinois	21,486	Edison, New Jersey*	18,197
Naperville, Illinois	21,000	Livingston, New Jersey*	18,176
Lake Zurich, Illinois	21,280	Moorestown, New Jersey	15,210
Lombard, Illinois	21,486	Rochelle Park, New Jersey	21,328
Schaumburg, Illinois	25,416	Cheektowaga, New York	25,532
Tinley Park, Illinois	22,100	Commack, New York	18,932
Indianapolis, Indiana	18,260	Rochester, New York	25,000
South Indy, Indiana	18,804	Scarsdale, New York	21,191
Des Moines, Iowa	24,960	Westbury, New York	17,704
Overland Park, Kansas	18,847	Charlotte, North Carolina	33,600
Shawnee, Kansas	19,032	Raleigh, North Carolina	22,213
Florence, Kentucky	27,752	Centerville, Ohio	28,440
Lexington, Kentucky	28,569	Columbus, Ohio	25,024
Louisville, Kentucky	20,000	Holland, Ohio*	32,312
Columbia, Maryland	21,350	North Olmsted, Ohio	20,000
Rockville, Maryland	34,478	Oakwood Village, Ohio	20,715
Timonium, Maryland*	20,000	Sharonville, Ohio	30,975
Avon, Massachusetts*	18,775	King of Prussia, Pennsylvania	25,522

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Ann Arbor, Michigan	28,188	Robinson, Pennsylvania	26,541
Bloomfield Hills, Michigan*	24,080	Knoxville, Tennessee	22,000
Farmington, Michigan	27,000	Nashville, Tennessee	18,147
Grand Rapids, Michigan	27,600	Glen Allen, Virginia	24,900
Sterling Heights, Michigan	29,520	Manassas, Virginia	26,568
Westland, Michigan	25,400	Springfield, Virginia	30,145
Bloomington, Minnesota	12,000	Sterling, Virginia	16,500
Burnsville, Minnesota	25,786	Virginia Beach, Virginia	22,000
Coon Rapids, Minnesota	24,186	Brown Deer, Wisconsin	19,848
Plymouth, Minnesota	30,500	Madison, Wisconsin	20,500
Roseville, Minnesota	29,412	West Allis, Wisconsin	22,932
Woodbury, Minnesota	18,731		

* We have signed leases for these locations, which we expect to open in 2012 or 2013.

We lease all of our stores. Our 10,000 square foot headquarters in Plymouth, Minnesota is attached to our flagship retail store. We own our three distribution centers, located in Spring Valley, Wisconsin; Ottawa Lake, Michigan; and Ridgeway, Virginia, which consist of 51,000, 271,000, and 100,000 square feet, respectively.

Legal Proceedings

From time to time, we have been and may become involved in legal proceedings arising in the ordinary course of our business. Although the results of litigation and claims cannot be predicted with certainty, we are not presently involved in any legal proceeding in which the outcome, if determined adversely to us, would be expected to have a material adverse effect on our business, operating results, or financial condition. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

MANAGEMENT

The following table provides information regarding our executive officers and directors, including their ages, as of September 30, 2012:

Name	Age	Position/Affiliation
Robert A. Rucker	60	Chief Executive Officer and President; Director
Timothy C. Clayton	57	Chief Financial Officer; Senior Vice President
Joseph Kinder	46	Senior Vice President - Operations
Carl Randazzo	47	Senior Vice President - Retail
Leigh M. Behrman	59	Vice President – Human Resources and Compliance
Peter J. Jacullo III(1)(2)	57	Director
Peter H. Kamin(1)(3)	50	Director
Todd Krasnow(2)(3)	54	Director
Adam L. Suttin(1)	44	Director
William E. Watts(2)	59	Director; Chairman of the Board

(1) Member of the audit committee

(2) Member of the compensation committee

(3) Member of the nominating and corporate governance committee

Robert A. Rucker has been our chief executive officer and president, and a member of our board of directors since June 2012. Previously, Mr. Rucker served as The Tile Shop's chief executive officer and president, and as a member of its board of managers. Mr. Rucker holds a B.E.S. in Psychology and History from the University of Minnesota. We believe that Mr. Rucker is qualified to serve on our board of directors based on his historic knowledge of The Tile Shop as its founder and his strategic vision for our Company.

Timothy C. Clayton has been our chief financial officer and senior vice president since August 2012. From June 2012 to August 2012, Mr. Clayton served as a financial consultant to The Tile Shop. Since June 2010, Mr. Clayton has also served as the chief financial officer of Sajan, Inc., a publicly-traded provider of language translation services and software. In addition, since September 2000, Mr. Clayton has been the principal of Emerging Capital, LLC, a management consulting firm, and, in such capacity, has served as the chief financial officer of ADESA, Inc., an automotive services company, and of other firms. Previously, from November 1997 to June 2000, Mr. Clayton was the chief financial officer of Building One Services Corporation, a publicly-traded facilities services company, of which he was also a co-founder. From August 1976 until November 1997, Mr. Clayton served in various capacities at Price Waterhouse, LLP, an independent public accounting firm, including serving as an audit and business advisory services partner from July 1988 to November 1997. Since January 2005, Mr. Clayton has been a director and

chairman of the audit committee of Agribank, FSB, a wholesale bank serving the rural agricultural market, and, since January 2003, Mr. Clayton has served on the board of directors of the National Federation of Independent Businesses, a nonpartisan lobbying organization. Mr. Clayton holds a B.A. in accounting from Michigan State University and is a certified public accountant.

Joseph Kinder has been our senior vice president — operations since June 2012. Previously, Mr. Kinder served as The Tile Shop's supply chain manager from August 1995 until June 2012, as an assistant store manager for The Tile Shop from March 1994 to August 1995, and as a sales person at The Tile Shop from March 1993 to March 1994. Mr. Kinder holds a B.A. in Business from the College of Saint Thomas.

Carl Randazzo has been our senior vice president — retail since June 2012. Previously, Mr. Randazzo served as The Tile Shop's national sales manager from October 2006 until June 2012, as a regional sales manager for The Tile Shop from June 2004 to October 2006, as a store manager for The Tile Shop from April 1994 to June 2004, and as a sales person at The Tile Shop from October 1992 to April 1994. Mr. Randazzo holds a B.S. in Economics from Arizona State University.

Leigh M. Behrman has been our vice president — human resources and compliance since June 2012. Previously, Mr. Behrman served as The Tile Shop's human resources manager from October 2007 until June 2012, as The Tile Shop's facility manager from June 1999 to October 2007, and as The Tile Shop's corporate controller from January 1988 to June 1999.

Each officer serves at the discretion of our board of directors and holds office until his or her successor is duly elected and qualified or until his or her earlier resignation or removal. There are no family relationships among any of our directors or executive officers.

Peter J. Jacullo III has served as a member of our board of directors since August 2012. Previously, Mr. Jacullo served as a member of The Tile Shop's board of managers from December 2007 to August 2012. Since July 1987, Mr. Jacullo has been a self-employed investor. Previously, Mr. Jacullo was a vice president and director of the Boston Consulting Group from May 1984 to July 1987, where he was also employed in various other capacities from May 1978 to May 1984. He is currently a director of ANZ Terminals Pty Limited, an Australian-based independent operator of bulk liquid and gas storage facilities with facilities located in Australia and New Zealand, and of Magnatech International Inc., a provider of equipment for the hydraulic hose industry. Mr. Jacullo holds an M.B.A. from the University of Chicago and a B.A. in Economics from Johns Hopkins University. We believe that Mr. Jacullo is qualified to serve on our board of directors in light of the continuity that he provides on our board of directors and his experience as a professional investor.

Peter H. Kamin has served as a member of our board of directors since August 2012. Previously, Mr. Kamin served as a member of The Tile Shop's board of managers from January 2012 to August 2012. Mr. Kamin has served as managing partner of 3K Limited Partnership, an investment fund, since January 2012. Previously, Mr. Kamin was the founding partner of ValueAct Capital, an investment fund, from January 2000 to January 2012. Since June 2012, Mr. Kamin has been a director and member of the audit committee of Ambassadors Group, Inc., a publicly-traded educational travel company; since May 2012, Mr. Kamin has been a director and member of the governance committee of MAM Software Group, Inc., a publicly-traded provider of business automation and ecommerce solutions for the automotive aftermarket; and since April 2012, Mr. Kamin has been a director and member of the audit committee of Rand Worldwide, Inc., a provider of technology solutions and professional services to engineering and design companies. Mr. Kamin previously served on the board of directors and as a member of the audit committee of Adesa, Inc., a publicly-traded provider of vehicle auction and remarketing services, from April 2007 to December 2011; on the board of directors and as a member of the audit and compensation committees of Seitel, Inc., a publicly-traded provider of onshore seismic data to the oil and gas industry, from February 2007 to December 2011; and on the board of directors and as a member of the governance committee of Exterran Holdings, Inc., a provider of natural gas compression products and services, from January 2007 to September 2008. Mr. Kamin holds an M.B.A. from the Harvard University Graduate School of Business and a B.A. in Economics from Tufts University. We believe that Mr. Kamin is qualified to serve on our board of directors due to his significant experience as a director of publicly-traded companies and his substantial experience as an investor.

Todd Krasnow has served as a member of our board of directors since August 2012. Previously, Mr. Krasnow served as a member of The Tile Shop's board of managers from January 2012 to August 2012. Mr. Krasnow has served as the president of Cobbs Capital, Inc., a private consulting company, since January 2005, and as marketing domain expert with Highland Consumer Fund, a venture capital firm, since June 2007. Previously, Mr. Krasnow was the chairman of Zoots, Inc., a dry cleaning company, from June 2003 to January 2008 and chief executive officer of Zoots, Inc. from February 1998 to June 2003. He served as the executive vice president of sales and marketing of Staples, Inc. from May 1993 to January 1998 and in other sales and marketing positions for Staples, Inc. from March 1986 to May 1993. Since September 2005, Mr. Krasnow has served as a director of Carbonite, Inc., a publicly-traded provider of online backup solutions for consumers and small and medium sized businesses; since December 2005, Mr. Krasnow has served as chairman of Carbonite's compensation committee and; since September 2009, he has served as a member of Carbonite's audit committee. Mr. Krasnow is also a director of OnForce, Inc., an online marketplace that enables enterprises to hire information technology service professionals, and Global Customer Commerce, Inc., an internet retailer of blinds and wall coverings; and a member of the advisory boards of C&S Wholesale Grocers, Inc. and Piedmont, Ltd., a Japanese storage company, which conducts business as Quraz. Mr. Krasnow holds an M.B.A. from the Harvard University Graduate School of Business and an A.B. in Chemistry from Cornell University. We believe that Mr. Krasnow is qualified to serve on our board of directors due to his operating and management experience and his expertise in sales and marketing.

Adam L. Suttin has served as a member of our board of directors since August 2012. Previously, Mr. Suttin served as president of JWC Acquisition Corp. Mr. Suttin co-founded J.W. Childs Associates, L.P., an private equity investment firm, in 1995 and is a partner of that firm. From 1989 to 1995, Mr. Suttin was an investment professional at Thomas H. Lee Company. He is currently a member of the board of directors of Brookstone, Inc., Refrigerator Manufacturers, Inc., Sunny Delight Beverages Co., Esselte Ltd., JA Apparel Corp. (Joseph Abboud), Mattress Firm Holdings, Inc., and The NutraSweet Company. Mr. Suttin hold a B.S. in Business from the Wharton School of the University of Pennsylvania and a B.A.S. in Engineering from the Moore School of Engineering of the University of Pennsylvania. We believe that Mr. Suttin is qualified to serve on our board of directors in light of his experience as a co-founder of J.W. Childs and his experience as a director of various companies.

William E. Watts has served as a member of our board of directors since August 2012. Previously, Mr. Watts served as vice president of JWC Acquisition Corp. Mr. Watts has been an operating partner of J. W. Childs Associates, L.P., an private equity investment firm, since June 2001. From 1991 to 2001, he was president and chief executive officer of General Nutrition Companies. Prior to being named president and chief executive officer, Mr. Watts held the positions of president and chief operating officer of General Nutrition, president and chief operating officer of General Nutrition Center, and senior vice president of retailing and vice president of retail operations of General Nutrition Center. Mr. Watts currently serves as chairman of the board of directors of Mattress Firm Holdings, Inc. and JA Apparel Corp. (Joseph Abboud), and is a member of the board of directors of Brookstone, Inc. Mr. Watts holds a B.A. in Social Science from the State University of New York at Buffalo. We believe that Mr. Watts is qualified to serve on our board of directors in light of his experience as a director of various companies and his experience as chief executive officer of a company with a well-known brand.

Classified Board of Directors

In accordance with our certificate of incorporation, our board of directors is divided into three classes with staggered three-year terms. At each annual meeting of stockholders, the successors to directors whose terms then expire will be elected to serve from the time of election and qualification until the third annual meeting following election. Except as otherwise provided by law and subject to the rights of any class or series of preferred stock, vacancies on our board of directors (including a vacancy created by an increase in the size of the board of directors) may be filled only by the affirmative vote of a majority of the remaining directors. A director elected by the board of directors to fill a vacancy (other than a vacancy created by an increase in the size of the board of directors) serves for the unexpired term of such director's predecessor in office and until such director's successor is elected and qualified. A director appointed to fill a position resulting from an increase in the size of the board of directors serves until the next annual meeting of stockholders at which the class of directors to which such director is assigned by the board of directors is to be elected by stockholders and until such director's successor is elected and qualified. Any additional directorships resulting from an increase in the number of directors will be distributed among the three classes so that, as nearly as possible, each class will consist of one-third of the directors.

Our directors are divided among the three classes as follows:

The Class I directors are Messrs. Jacullo and Suttin, with terms expiring at the annual meeting of stockholders to be held in 2013;

The Class II directors are Messrs. Kamin and Krasnow, with terms expiring at the annual meeting of stockholders to be held in 2014; and

The Class III directors are Messrs. Rucker and Watts, with terms expiring at the annual meeting of stockholders to be held in 2015.

Independence of the Board of Directors

As required under the rules and regulations of the Nasdaq Stock Market, or Nasdaq, independent directors must comprise a majority of a listed company's board of directors. Based upon information requested from and provided by each director concerning his background, employment, and affiliations, including family relationships, we have determined that Messrs. Jacullo, Kamin, Krasnow, Suttin, and Watts, representing five of our six directors, do not have a relationship that would interfere with the exercise of independent judgment in carrying out the responsibilities of a director and that each of these directors will be "independent" as that term is defined under the applicable rules and regulations of the Securities and Exchange Commission, or the SEC, and the listing requirements and rules of Nasdaq.

Committees of the Board of Directors

Our board of directors has established the following committees: an audit committee, a compensation committee, and a nominating and corporate governance committee. The composition and responsibilities of each committee are described below. Members serve on these committees until their resignation or until otherwise determined by our board of directors.

Audit Committee

Our audit committee oversees our corporate accounting and financial reporting process, the audit of our financial statements, and our internal control processes. Among other matters, the audit committee evaluates our independent auditors' qualifications, independence, and performance; determines the engagement, retention, and compensation of the independent auditors; reviews and approves the scope of the annual audit and the audit fee; discusses with management and the independent auditors the results of the annual audit and the review of our quarterly financial statements, including the disclosures in our annual and quarterly reports to be filed with the SEC; approves the retention of the independent auditors to perform any proposed permissible non-audit services; reviews our risk assessment and risk management processes; establishes procedures for receiving, retaining, and investigating complaints received by us regarding accounting, internal accounting controls, or audit matters; monitors the rotation of partners of the independent auditors on our engagement team as required by law; reviews our critical accounting policies and estimates; and oversees any internal audit function. Additionally, the audit committee reviews and approves related person transactions and reviews and evaluates, on an annual basis, the audit committee charter and the committee's performance.

The current members of our audit committee are Messrs. Jacullo, Kamin, and Suttin, with Mr. Kamin serving as the chair of the committee. All members of our audit committee meet the requirements for financial literacy under the applicable rules and regulations of the SEC and Nasdaq. Our board of directors has determined that Mr. Kamin is an

audit committee financial expert as defined under the applicable rules of the SEC and has the requisite financial sophistication as defined under the applicable rules and regulations of Nasdaq. Messrs. Jacullo, Kamin, and Krasnow are independent directors as defined under the applicable rules and regulations of the SEC and Nasdaq. The audit committee operates under a written charter that satisfies the applicable standards of the SEC and Nasdaq.

Compensation Committee

Our compensation committee reviews and recommends policies relating to compensation and benefits of our executive officers and employees. The compensation committee annually reviews and approves corporate goals and objectives relevant to compensation of our chief executive officer and other executive officers, evaluates the performance of these officers in light of those goals and objectives, and sets the compensation of these officers based on such evaluations. The compensation committee also administers the issuance of stock options and other awards under our equity compensation plans. Additionally, the compensation committee reviews and evaluates, on an annual basis, the compensation committee charter and the committee's performance.

The current members of our compensation committee are Messrs. Jacullo, Krasnow, and Watts, with Mr. Krasnow serving as the chair of the committee. All of the members of our compensation committee are independent under the applicable rules and regulations of the SEC, Nasdaq, and Section 162(m) of the Internal Revenue Code of 1986, as amended (the “Code”). The compensation committee operates under a written charter.

Nominating and Corporate Governance Committee

Our nominating and corporate governance committee is responsible for making recommendations regarding corporate governance; identification, evaluation and nomination of candidates for directorships; and the structure and composition of our board of directors and committees thereof. In addition, the nominating and corporate governance committee oversees our corporate governance guidelines, approves our committee charters, oversee compliance with our code of business conduct and ethics, contributes to succession planning, reviews actual and potential conflicts of interest of our directors and officers other than related person transactions reviewed by the audit committee, and oversees the board of directors self-evaluation process. Our nominating and corporate governance committee is also responsible for making recommendations regarding non-employee director compensation to the full board of directors. Additionally, the nominating and corporate governance committee reviews and evaluates, on an annual basis, the nominating and corporate governance committee charter and the committee’s performance.

The current members of our nominating and corporate governance committee are Messrs. Kamin and Krasnow, with Mr. Krasnow serving as the chair of the committee. All of the members of our nominating and corporate governance committee are independent under the applicable rules and regulations of Nasdaq. The nominating and corporate governance committee operates under a written charter.

Compensation Committee Interlocks and Insider Participation

We had no compensation committee nor committee of the board of directors performing an equivalent function during the fiscal year ended December 31, 2011. None of the individuals who currently serves as a member of our compensation committee (i) are, or at any time during the past year or our last completed fiscal year have been, officers or directors of ours, (ii) were formerly officers or directors of our, or (iii) have had any relationship requiring disclosure by us under Item 404 of Regulation S-K. None of our executive officers currently serves, nor in the past year has served, as a member of the board of directors or compensation committee (or other board committee performing equivalent functions) of any entity that has one or more executive officers serving on our board of directors or compensation committee. During the fiscal year completed December 31, 2011, none of The Tile Shop’s executive officers or employees, other than Mr. Rucker, participated in the deliberations of The Tile Shop’s board of managers concerning executive officer compensation.

Involvement in Certain Legal Proceedings

In October 2011, Mr. Kinder was involved in a domestic dispute (misdemeanor charge stayed) and a verbal altercation with police officers in front of his family (pled guilty to a gross misdemeanor).

Code of Business Conduct and Ethics

We have adopted a code of business conduct and ethics that applies to all of our employees, officers, and directors, including those officers responsible for financial reporting. The code of business conduct and ethics is available on our website at www.tileshop.com. We expect that, to the extent required by law, any amendments to the code, or any waivers of its requirements, will be disclosed on its website.

Director Compensation

Prior to consummation of the Business Combination, we paid each of Messrs. Kamin and Krasnow \$50,000 per year for service on The Tile Shop's board of managers and, in January 2012, granted to each of Messrs. Kamin and Krasnow 116,750 Series 2012 Participating Capital Appreciation Common Units, or Series 2012 Units, of The Tile Shop. The Series 2012 Units shared ratably with The Tile Shop's common unit membership interests, or Common Units, in distributions from The Tile Shop after a certain aggregate distribution threshold had been reached with regard to the Common Units. In January 2012, Mr. Kamin transferred the Series 2012 Units held by him to the Peter H. Kamin GST Trust, of which Mr. Kamin is a trustee. The Series 2012 Units vested in full immediately prior to the consummation of the Business Combination and each of Mr. Krasnow and the Peter H. Kamin GST Trust shared ratably in the consideration payable to the former direct and indirect members of The Tile Shop in connection with the Business Combination as though each such holder's Series 2012 Units were converted into 41,564 Common Units.

We did not pay any compensation to the members of The Tile Shop's board of managers for the year ended December 31, 2011, other than to Mr. Rucker in his capacity as president and chief executive officer of The Tile Shop.

Each of our non-employee directors receives an annual fee of \$100,000 and the chairperson of our board of directors receives an additional annual fee of \$150,000. The fees for the current year were paid upon the consummation of the Business Combination in the form of restricted common stock valued at \$10.00 per share and granted pursuant to our 2012 Equity Award Plan, or 2012 Plan. In each subsequent year, we expect that each non-employee director and the chairperson of our board of directors will receive the fees payable to them in their capacities as such one-half in cash and one-half in the form of restricted common stock granted pursuant to the 2012 Plan or a successor plan thereto. The number of shares of our restricted common stock to be granted in each subsequent year will be equal to the quotient obtained by dividing (i) the amount of the annual fee payable to such non-employee director in the form of restricted stock, as set forth above, by (ii) the average closing price on Nasdaq of our common stock over 30 trading days immediately preceding the date of grant. The restricted stock grants for the current year and for each subsequent year will vest in full on the first anniversary of the date of grant, contingent upon the applicable non-employee director's continued service on our board of directors.

Notwithstanding the foregoing, each of Messrs. Jacullo and Suttin have agreed to forego all compensation for their service as directors of our Company.

EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

This section discusses the principles our policies and decisions with respect to the compensation of our executive officers and employees who are named in the “2011 Summary Compensation Table” and the most important factors relevant to an analysis of these policies and decisions. These “named executive officers,” who were executive officers of The Tile Shop during 2011, are:

- Robert A. Rucker, chief executive officer;
- Joseph Kinder, senior vice president - operations;
- Carl Randazzo, senior vice president - retail; and
- Leigh M. Behrman, vice president – human resources and compliance.

We expect that our executive compensation philosophy as a publicly traded company will differ from our historical compensation philosophy as a result on our compensation committee’s continued review and evaluation of our compensation philosophy and structure.

Overview

We recognize that our ability to excel depends on the integrity, knowledge, imagination, skill, diversity, and teamwork of our employees. To this end, we strive to create an environment of mutual respect, encouragement, and teamwork that rewards commitment and performance and that is responsive to the needs of our employees. The principles and objectives of our compensation and benefits programs for our employees generally, and for our named executive officers specifically, are to:

· align compensation incentives with our corporate strategies, business, and financial objectives and the long-term interests of our stockholders;

- motivate and reward executives whose knowledge, skills, and performance ensure our continued success; and
- ensure that total compensation is fair, reasonable, and competitive.

Historically, the compensation for our named executive officers has consisted of (i) base salary, (ii) performance bonus, (iii) phantom equity units, (iii) perquisites and health and welfare benefits, and (v) 401(k) plan retirement savings opportunities. Effective immediately prior to the consummation of the Business Combination, we terminated our historical Deferred Compensation Plan, pursuant to which we previously granted phantom equity units, and anticipate that we will make a lump-sum cash payment to each former holder of phantom equity units, including certain of our named executive officers, on August 20, 2013 in full satisfaction of all phantom equity units previously held by such individuals.

Effective upon consummation of the Business Combination, we adopted the 2012 Plan, and made grants to certain of our named executive officers thereunder. For a further description of the 2012 Plan, see “Executive Compensation – Compensation Discussion and Analysis — Executive Compensation Program Components — 2012 Equity Award Plan” beginning on page 59 of this prospectus.

Each of the primary elements of our executive compensation program are discussed in more detail below. While we have identified particular compensation objectives that each element of executive compensation serves, our compensation programs are designed to be flexible and complementary and to collectively serve all of the executive compensation objectives described above. Accordingly, whether or not specifically mentioned below, we believe that each individual element, to some extent, serves each of our objectives. Further, while each of our executive officers has not been, and will not be, compensated with all individual compensation elements, we believe that the compensation provided to each individual executive officer is, and will be, consistent with the overall compensation philosophy and objectives set forth above.

Compensation Determination Process

As we transition from being a privately held company to a publicly traded company, we will evaluate our philosophy and compensation programs as circumstances require and, at a minimum, we will review executive compensation annually. As part of this review process, we expect to apply the values and the objectives outlined above, together with consideration for the levels of compensation that we would be willing to pay to ensure that our compensation remains competitive and that it is meeting our retention objectives in light of the cost to us if we were required to replace a key employee.

Historically, The Tile Shop's board of managers did not review anonymous private company compensation surveys in setting the compensation of our named executive officers. In the future, we anticipate that our compensation committee will determine executive compensation, at least in part, by reference to the compensation information for the executives of a peer group of comparable companies, although no such peer group has yet been determined. Additionally, our compensation committee plans to engage a compensation consultant to provide market data on a peer group of companies in our industry on an annual basis, and we intend to review this information and other information obtained by the members of our compensation committee to help ensure that our compensation program is competitive. We anticipate that our compensation committee may make adjustments in executive compensation levels in the future as a result of this more formal market comparison process.

The compensation levels of our named executive officers reflect, to a significant degree, the varying roles and responsibilities of such executives. As a result of our board of directors and The Tile Shop's board of managers, as applicable, assessment of Robert Rucker's roles and responsibilities, there is and has been a significant compensation differential between his compensation levels and those of our other named executive officers.

Executive Compensation Program Components

Base Salary

In general, base salaries of our named executive officers were initially established through arm's-length negotiation at the time the executive was hired, taking into account such executive's qualifications, experience, and prior salary. Base salaries of our named executive officers are approved and reviewed periodically by our chief executive officer, and in the case of our chief executive officer's base salary, by our board of directors or The Tile Shop's board of managers, as applicable, and adjustments to base salaries are based on the scope of an executive's responsibilities, individual contribution, prior experience, and sustained performance. Decisions regarding salary increases may take into account the executive officer's current salary, equity or equity-linked interests, and the amounts paid to an executive officer's peers within our Company. In making decisions regarding salary increases, we may also draw upon the experience of members of our board of directors with other companies. Base salaries are also reviewed in the case of promotions or other significant changes in responsibility. No formulaic base salary increases are provided to our named executive officers. This strategy is consistent with our intent of offering base salaries that are cost-effective while remaining competitive.

The actual base salaries earned by all of our named executive officers, who were executive officers of The Tile Shop in 2011, are set forth in the "2011 Summary Compensation Table."

In anticipation of the consummation of the Business Combination, we entered into offer letter agreements with each of Messrs. Rucker, Kinder, Randazzo, and Behrman, which provide for annual base salaries of \$303,991, \$200,000, \$200,000, and \$119,000, respectively. Pursuant to the terms of his offer letter, Mr. Rucker's base salary will be increased to \$500,000 effective January 1, 2013. We also entered into an offer letter agreement with Timothy C. Clayton, our chief financial officer and senior vice president, which provides for an annual base salary of \$200,000. For a further description of these offer letter agreements, see "Executive Compensation — Offer Letter Agreements" beginning on page 67 of this prospectus.

Annual Cash Bonuses

Historically, annual cash bonuses have been awarded to our named executive officers when The Tile Shop's board of managers or our chief executive officer determined that such bonuses were merited in light of corporate performance.

Mr. Rucker has historically been awarded an annual cash bonus in an amount sufficient to provide Mr. Rucker with total actual after-tax bonus compensation equal to 3% of our net income, inclusive of the bonus compensation and associated tax adjustment payable to Mr. Rucker, for the corresponding period. Our other named executive officers have historically been awarded annual cash bonuses in an amount determined by our chief executive officer and approved by our board of directors or The Tile Shop's board of managers, as applicable, reflecting (i) our annual operating performance, (ii) our year-over-year operating growth, (iii) attainment of individual and corporate goals, and (iv) other discretionary factors deemed relevant.

The actual cash bonuses earned by all of our named executive officers, who were executive officers of The Tile Shop in 2011, are set forth in the "2011 Summary Compensation Table."

Going forward, our compensation committee intends to adopt a cash bonus program for our executive officers, other than Messrs. Rucker and Clayton, pursuant to which each of our executive officers will be eligible to receive bonus compensation in an amount up to 50% of his base salary, subject to attainment of corporate and individual performance targets that will be established by our compensation committee and approved by our board of directors prior to the beginning of each fiscal year. This cash bonus program is expected to become effective for 2013.

We intend to continue Mr. Rucker's historical bonus compensation arrangement for 2012. Effective for 2013, we intend to provide Messrs. Rucker and Clayton with target cash bonus compensation equal to 100% and 50%, respectively, of his base salary based on our Adjusted EBITDA for the year. Messrs. Rucker's and Clayton's respective target bonus compensation would be earned if we achieve the Adjusted EBITDA target set forth in our budget. Messrs. Rucker and Clayton would each be entitled to receive a partial bonus payment if we partially achieves our budgeted Adjusted EBITDA, and a bonus in excess of the target bonus amount if we achieve greater than 100% of our budgeted Adjusted EBITDA. Messrs. Rucker and Clayton would each earn a partial bonus payment if we achieve at least 85% of our budgeted Adjusted EBITDA target and an additional bonus of up to double his target amount if we achieve 115% of our budgeted Adjusted EBITDA, with the actual bonus amounts that Messrs. Rucker and Clayton would be entitled to receive within this range to be determined by our compensation committee.

Equity and Equity-Linked Incentives

Historically, in order to align the interests of our named executive officers with those of our stockholders, we granted certain of our employees and each of our named executive officers, other than Mr. Rucker, phantom equity units pursuant our Deferred Compensation Plan that were payable in cash based on the appreciation in the value of The Tile Shop's Common Units. Due to Mr. Rucker's significant beneficial equity interest in The Tile Shop, The Tile Shop's board of managers determined that it was not necessary or appropriate to grant Mr. Rucker any such phantom equity units. These phantom equity units were fully-vested upon grant and payable to the holders thereof upon the earlier of (i) the tenth or fifteenth anniversary of the date of grant, as applicable, or (ii) immediately prior to a change of control of The Tile Shop. Upon the occurrence of either such event, the holder of each unit of phantom equity is entitled to receive, in respect of each such unit, a payment in cash equal to the change in the fair market value of The Tile Shop's Common Units between the date of grant and (a) the last day of the fiscal year immediately preceding the tenth or fifteenth anniversary of the date of grant, as applicable, or (b) the date of the change of control, as applicable. At all times from January 1, 2009 until the termination of our Deferred Compensation Plan in connection with the consummation of the Business Combination, Messrs. Behrman, Kinder, and Randazzo held 100,000, 300,000, and 300,000 phantom equity units of The Tile Shop, respectively. Effective immediately prior to the consummation of the Business Combination, we terminated our Deferred Compensation Plan and anticipate that we will make a lump-sum cash payment to each former holder of phantom equity units, including Messrs. Behrman, Kinder, and Randazzo, on August 20, 2013 in full satisfaction of all phantom equity units previously held by such individuals. Messrs. Behrman, Kinder, and Randazzo will receive payments of \$824,000, \$2,060,000, and \$2,060,000, respectively, on such date.

Going forward, we intend to use equity incentive awards pursuant to our 2012 Plan to continue to tie the interests of our named executive officers with those of our stockholders. Vesting of these equity incentive awards, which we expect to be primarily in the form of stock option grants for our named executive officers other than Mr. Rucker, will be based in whole or in part on continued employment to encourage the retention of our named executive officers through the vesting period of the awards, and, in some cases, partially based on the annual appreciation of our common stock. In determining the size of both the initial and “refresher” equity awards to our named executive officers, our compensation committee intends to take into account a number of internal factors, such as the relative job scope, the value of outstanding equity awards, individual performance history, prior contributions to us, and the size of prior awards, as well as external factors such as the levels of unvested equity awards held by our executive officers in relation to their peers at comparable companies.

In August 2012, upon the consummation of the Business Combination, Messrs. Kinder, Randazzo, Clayton, and Behrman received initial grants of options to purchase 330,000, 330,000, 220,000, and 110,000 shares of our common stock, respectively, at an exercise price per share of \$10.00. Two-thirds of the total number of shares subject to each such stock option grant are subject to vesting in equal annual installments over four years from the date of grant, based only upon the applicable executive officer’s continued service to us, and that one-third of the total number of shares subject to each such stock option grant will be subject to vesting in equal annual installments over four years from the date of grant, based both on the appreciation in the price of our common stock and continued service to us. The portion of stock option grants tied to appreciation in the price of our common stock will vest on each anniversary of the date of grant, subject to a 20% increase in the trading price of our common stock over the applicable one-year period, which increase will be measured by reference to the average closing price on the Nasdaq Stock Market of our common stock over the 30 trading days immediately preceding the date of grant or anniversary date thereof, as applicable. We believe that these vesting schedules will appropriately encourage long-term employment with us while allowing our executives to realize compensation in line with the value that they create for our stockholders.

In August 2012, upon the consummation of the Business Combination, we also granted to Mr. Rucker an award of 250,000 restricted shares of our common stock, which award will vest and become unrestricted as to one-third of the total number of shares of common stock on each of December 31, 2013, 2014, and 2015, subject to Mr. Rucker’s continued service as an employee, officer, or director of our Company.

We have provided for the acceleration of vesting of equity awards granted to each of Messrs. Rucker, Clayton, Kinder, Randazzo, and Behrman in the event of a change of control of our Company. In the event of a change of control, if the individual is terminated without cause or is otherwise constructively terminated prior to the first anniversary of the change of control, the vesting of any unvested awards will be accelerated in full immediately prior to such termination. We believe that these acceleration opportunities will further align the interests of our executives with those of our stockholders by providing our executives an opportunity to benefit alongside our stockholders in a corporate transaction.

We do not have any securities ownership requirements for our named executive officers.

2012 Equity Award Plan

In June 2012, our board of directors and stockholders adopted the 2012 Plan, which became effective upon the consummation of the Business Combination. The principal purpose of the 2012 Plan is to attract, retain, and motivate selected employees, consultants, and directors through the granting of stock-based compensation awards.

The principal features of the 2012 Plan are summarized below. This summary is qualified in its entirety by reference to the text of the 2012 Plan, which was filed as an exhibit to our registration statement on Form S-4 (File No. 333-182482), which is amended hereby.

Share reserve

Under the 2012 Plan, 2,500,000 shares of our common stock were initially reserved for issuance pursuant to a variety of stock-based compensation awards, including stock options and restricted stock awards. The number of shares initially reserved for issuance or transfer pursuant to awards under the 2012 Plan will be increased on the first day of each calendar year beginning in 2013 and ending in 2022, in an amount equal to the least of (A) 2,500,000 shares, (B) six percent (6%) of the shares of common stock outstanding (on an as-converted basis) on the last day of the immediately preceding calendar year, and (C) such smaller number of shares of common stock as determined by our board of directors.

The following counting provisions are in effect for the share reserve under the 2012 Plan:

to the extent that an award terminates, expires, or lapses for any reason, any shares subject to the award at such time will be available for future grants under the 2012 Plan, provided that no such shares may be issued pursuant to an incentive stock option;

to the extent shares are tendered or withheld to satisfy the grant, exercise price, or tax withholding obligation with respect to any award under the 2012 Plan, such tendered or withheld shares will be available for future grants under the 2012 Plan, provided that no such shares may be issued pursuant to an incentive stock option; and

to the extent permitted by applicable law or any exchange rule, shares issued in assumption of, or in substitution for, any outstanding awards of any entity acquired in any form of combination by us or any of our subsidiaries will not be counted against the shares available for issuance under the 2012 Plan.

Notwithstanding the foregoing, no individual may be granted stock-based awards under the 2012 Plan covering more than 2,000,000 shares in any calendar year.

As of September 30, 2012, 2,050,000 shares of common stock were subject to outstanding awards pursuant to the 2012 Plan.

Administration

The compensation committee of our board of directors administers the 2012 Plan, subject to the right of our board of directors to assume authority for administration or delegate such authority to another committee of the board of directors. The compensation committee must consist of at least two members of our board of directors, each of whom is intended to qualify as an “outside director,” within the meaning of Section 162(m) of the Code, a “non-employee director” for purposes of Rule 16b-3 under the Securities Exchange Act of 1934, as amended, or the Exchange Act, and an “independent director” within the meaning of the rules of the Nasdaq Stock Market, or other principal securities market on which shares of our common stock are traded. The composition of our compensation committee meets these requirements. The 2012 Plan provides that the compensation committee may delegate its authority to grant awards to employees other than executive officers and certain senior executives of our Company to one or more of our officers.

Subject to the terms and conditions of the 2012 Plan, the administrator has the authority to select the persons to whom awards are to be made, to determine the number of shares to be subject to awards and the terms and conditions of awards, and to make all other determinations and to take all other actions necessary or advisable for the administration of the 2012 Plan. The administrator is also authorized to adopt, amend, or rescind rules relating to administration of the 2012 Plan. Our board of directors may at any time remove the compensation committee as the administrator and revest in itself the authority to administer the 2012 Plan. The full board of directors will administer the 2012 Plan with respect to awards to non-employee directors.

Eligibility

Awards under the 2012 Plan may be granted to individuals who are then our officers, employees, directors, or consultants or are the officers, employees, directors, or consultants of our subsidiaries. Only executive officers and employees may be granted incentive stock options, or ISOs.

Awards

The 2012 Plan provides that the administrator may grant or issue stock options and restricted stock or any combination thereof. Each award will be set forth in a separate agreement with the person receiving the award and will indicate the type, terms, and conditions of the award.

Nonqualified stock options, or NQSOs, provide for the right to purchase shares of our common stock at a specified price that may not be less than fair market value on the date of grant, and usually will become exercisable (at the discretion of the administrator) in one or more installments after the grant date, subject to the participant's continued employment or service with us or a subsidiary and/or subject to the satisfaction of corporate performance targets and individual performance targets established by the administrator. NQSOs may be granted for any term specified by the administrator, but may not exceed ten years.

Incentive stock options are designed in a manner intended to comply with the provisions of Section 422 of the Code and will be subject to specified restrictions contained in the Code. Among such restrictions, ISOs must have an exercise price of not less than the fair market value of a share of common stock on the date of grant, may only be granted to employees, and must not be exercisable after a period of ten years measured from the date of grant. In the case of an ISO granted to an individual who owns (or is deemed to own) at least 10% of the total combined voting power of all classes of our capital stock, the 2012 Plan provides that the exercise price must be at least 110% of the fair market value of a share of common stock on the date of grant and that the ISO must not be exercisable after a period of five years measured from the date of grant.

Restricted stock may be granted to any eligible individual and made subject to such restrictions as may be determined by the administrator. Restricted stock, typically, may be forfeited for no consideration or repurchased by us at the original purchase price if the conditions or restrictions on vesting are not met. In general, restricted stock may not be sold, or otherwise transferred, until restrictions are removed or expire. Purchasers of restricted stock, unlike recipients of options, will have voting rights and will have the right to receive dividends, if any, prior to the time when the restrictions lapse.

Change of control

In the event of a change of control, the administrator may, in its sole discretion, accelerate vesting of awards issued under the 2012 Plan such that 100% of any such award may become vested and exercisable. Additionally, the administrator has complete discretion to structure one or more awards under the 2012 Plan to provide that such awards will become vested and exercisable on an accelerated basis. The administrator may also make appropriate adjustments to awards under the 2012 Plan and is authorized to provide for the acceleration, termination, assumption, substitution, or conversion of such awards in the event of a change of control or certain other unusual or nonrecurring events or transactions. Under the 2012 Plan, a change of control is generally defined as:

the transfer or exchange in a single or series of related transactions by our stockholders of more than 50% of our voting securities to a person or group;

a change in the composition of our board of directors over a two-year period such that 50% or more of the members of the board were elected through one or more contested elections;

a merger, consolidation, reorganization, or business combination in which we are involved, directly or indirectly, other than a merger, consolidation, reorganization, or business combination which results in our outstanding voting securities immediately before the transaction continuing to represent a majority of the voting power of the acquiring company's outstanding voting securities and after which no person or group beneficially owns 50% or more of the outstanding voting securities of the surviving entity immediately after the transaction;

the sale, exchange, or transfer of all or substantially all of our assets; or

stockholder approval of our liquidation or dissolution.

Adjustments of awards

In the event of any stock dividend, stock split, extraordinary cash dividend, combination or exchange of shares, merger, consolidation, spin-off, recapitalization, distribution of our assets to stockholders, or any other corporate event affecting the number of outstanding shares of our common stock or the share price of our common stock that would require adjustments to the 2012 Plan or any awards under the 2012 Plan in order to prevent the dilution or enlargement of the potential benefits intended to be made available thereunder, the administrator will make appropriate, proportionate adjustments to:

the aggregate number and type of shares subject to the 2012 Plan;

the terms and conditions of outstanding awards (including, without limitation, any applicable performance targets or criteria with respect to such awards);

the grant or exercise price per share of, and the aggregate number of shares subject to, any outstanding awards under the 2012 Plan; and

the performance goals pertaining to any award.

Amendment and termination

Our board of directors or the compensation committee (with board approval) may terminate, amend, or modify the 2012 Plan at any time and from time-to-time. However, we must generally obtain stockholder approval:

- to increase the number of shares available under the 2012 Plan (other than in connection with certain corporate events, as described above);

- to expand the group of participants under the 2012 Plan;

- to diminish the protections afforded by the 2012 Plan with regard to decreasing the exercise price for options or otherwise materially change the vesting or performance requirements of an award; or

- to the extent required by applicable law, rule, or regulation (including any applicable stock exchange rule).

Notwithstanding the foregoing, no option may be amended to reduce the per share exercise price below the per share exercise price of such option on the grant date and no options may be granted in exchange for, or in connection with, the cancellation or surrender of options having a higher per share exercise price without receiving additional stockholder approval.

Expiration date

The 2012 Plan will expire on, and no option or other award may be granted pursuant to the 2012 Plan after, August 21, 2022. Any award that is outstanding on the expiration date of the 2012 Plan will remain in force according to the terms of the 2012 Plan and the applicable award agreement.

Securities laws and federal income taxes

The 2012 Plan is designed to comply with certain securities and federal tax laws, including as follows:

Securities laws. The 2012 Plan is intended to conform to all provisions of the Securities Act and the Exchange Act and any and all regulations and rules promulgated by the SEC thereunder, including, without limitation, Rule 16b-3. The 2012 Plan will be administered, and options will be granted and may be exercised, only in such a manner as to conform to such laws, rules, and regulations.

Section 409A of the Internal Revenue Code. Certain awards under the 2012 Plan may be considered “nonqualified deferred compensation” for purposes of Section 409A of the Code, which imposes certain additional requirements regarding the payment of deferred compensation. Generally, if at any time during a taxable year a nonqualified deferred compensation plan fails to meet the requirements of Section 409A, or is not operated in accordance with those requirements, all amounts deferred under such plan and all other equity incentive plans for the taxable year and all preceding taxable years, by any participant with respect to whom the failure relates, are includible in gross income for the taxable year to the extent not subject to a substantial risk of forfeiture and not previously included in gross income. If a deferred amount is required to be included in income under Section 409A, the amount also is subject to interest and an additional income tax. The interest imposed is equal to the interest at the underpayment rate plus one percentage point, imposed on the underpayments that would have occurred had the compensation been includible in income for the taxable year when first deferred, or if later, when not subject to a substantial risk of forfeiture. The additional federal income tax is equal to 20% of the compensation required to be included in gross income. In addition, certain states, including California, have laws similar to Section 409A, which impose additional state penalty taxes on such compensation.

Section 162(m) of the Internal Revenue Code. In general, under Section 162(m) of the Code, income tax deductions of publicly-held corporations may be limited to the extent total compensation (including, but not limited to, base salary, annual bonus, and income attributable to stock option exercises and other non-qualified benefits) for certain executive officers exceeds \$1,000,000 (less the amount of any “excess parachute payments” as defined in Section 280G of the Code) in any taxable year of the corporation. However, under Section 162(m), the deduction limit does not apply to certain “performance-based compensation” established by an independent compensation committee that is adequately disclosed to, and approved by, stockholders. In particular, stock options granted pursuant to the 2012 Plan will satisfy the “performance-based compensation” exception if the awards are made by a qualifying compensation

committee, the 2012 Plan sets the maximum number of shares that can be granted to any person within a specified period, and the compensation is based solely on an increase in the stock price after the grant date. Specifically, the option exercise price must be equal to or greater than the fair market value of the stock subject to the award on the grant date. Under a Section 162(m) transition rule for compensation plans of corporations which are privately-held and which become publicly-held in a business combination, the 2012 Plan will not be subject to Section 162(m) until a specified transition date, which is the earlier of:

· the first material modification of the 2012 Plan;

· the issuance of all of the shares of our common stock reserved for issuance under the 2012 Plan;

· the expiration of the 2012 Plan; or

the first meeting of our stockholders at which members of our board of directors are to be elected that occurs after the close of the third calendar year following the calendar year in which the Business Combination occurred.

After the transition date, awards granted under the 2012 Plan, other than options, will not qualify as “performance-based compensation” for purposes of Section 162(m) unless such rights or awards are granted or vest upon pre-established objective performance goals, the material terms of which are disclosed to and approved by our stockholders. Thus, we expect that such other rights or awards under the 2012 Plan will not constitute performance-based compensation for purposes of Section 162(m).

We have attempted to structure the 2012 Plan in such a manner that, after the transition date the compensation attributable to stock options, and other performance-based awards which meet the other requirements of Section 162(m) will not be subject to the \$1,000,000 limitation. We have not, however, requested a ruling from the IRS or an opinion of counsel regarding this issue.

On August 21, 2012, we filed with the SEC a registration statement on Form S-8 covering the shares of our common stock issuable under the 2012 Plan.

Retirement savings

All of our full-time employees, including our named executive officers, are eligible to participate in The Tile Shop 401(k) plan. Employees may elect to reduce their current compensation by up to the statutorily prescribed annual limit, which was \$16,500 in 2011, and to have the amount of this reduction contributed to the 401(k) plan. In 2011, we made a matching contribution of \$0.25 for every \$1.00 that each applicable employee contributed to the 401(k) plan, up to a maximum of 5% of such employee’s salary. Each year, this matching contribution vests as to 20% of the aggregate matching contributions for such employee, such that all previous and future matching contributions will be vested after the employee has been employed by us for a period of five years.

Perquisites

From time-to-time, we have provided certain of our named executive officers with perquisites that we believe are reasonable. We do not view perquisites as a significant element of our comprehensive compensation structure, but do believe they can be useful in attracting, motivating, and retaining executive talent. We believe that these additional benefits may assist our executive officers in performing their duties and provide time efficiencies for our executive officers in appropriate circumstances, and may consider providing additional perquisites in the future. There are no material perquisites to our named executive officers that are contractual obligations pursuant to written agreement. All

future practices regarding perquisites will be approved and subject to periodic review by our compensation committee.

Tax considerations

Our board of directors will consider the potential future effects of Section 162(m) of the Code on the compensation paid to our executive officers. Section 162(m) disallows a tax deduction for any publicly-held corporation for individual compensation exceeding \$1.0 million in any taxable year for the chief executive officer and each of the next three most highly compensated executive officers (other than the chief financial officer, if any), unless the compensation is “performance based” or based on another available exemption. Prior to being a publicly-held corporation, The Tile Shop’s board of managers did not take the deductibility limit imposed by Section 162(m) into consideration in setting compensation. We expect that our compensation committee will adopt a policy that, where reasonably practicable, will seek to qualify the variable compensation paid to our executive officers for an exemption from the deductibility limitations of Section 162(m). As such, in approving the amount and form of compensation for our executive officers in the future, our compensation committee will consider all elements of the cost to us of providing such compensation, including the potential impact of Section 162(m). However, our compensation committee may, in its judgment, authorize compensation payments that do not comply with the exemptions in Section 162(m) when it believes that such payments are appropriate to attract and retain executive talent.

Taxation of “parachute” payments and deferred compensation

We did not provide any executive officer, including any named executive officer, with a “gross-up” or other reimbursement payment for any tax liability that he or she might owe as a result of the application of Sections 409A of the Code during 2011, and we have not agreed, nor are otherwise obligated, to provide any executive officer with such a “gross-up” or other reimbursement. Sections 280G and 4999 of the Code provide that executive officers and directors who hold significant equity interests and certain other service providers may be subject to an excise tax if they receive payments or benefits in connection with a change of control that exceeds certain prescribed limits, and that we, or a successor, may forfeit a deduction on the amounts subject to this additional tax. Section 409A of the Code also imposes additional significant taxes on the individual in the event that an executive officer, director, or other service provider received “deferred compensation” that does not meet the requirements of Section 409A of the Code.

2011 Summary Compensation Table

The following table summarizes the compensation earned by each of Messrs. Rucker, Kinder, Randazzo, and Behrman during the fiscal year ended December 31, 2011:

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Non-Equity Incentive Plan Compensation (\$)	All Other Compensation (\$)	Total (\$)
Robert A. Rucker, <i>Chief Executive Officer</i>	2011	262,302	1,032,971	-	788,144 (1)	2,083,417
Joseph Kinder, <i>Senior Vice President - Operations</i>	2011	162,000	91,345	470,000	-	723,345
Carl Randazzo, <i>Senior Vice President - Retail</i>	2011	162,000	135,227	470,000	-	767,227
Leigh M. Behrman, <i>Vice President – Human Resources and Compliance</i>	2011	119,000	45,402	220,000	-	384,402

(1) Includes \$782,444 in tax “gross-ups” related to Mr. Rucker’s bonus compensation and \$5,700 in insurance premiums payments made on behalf of Mr. Rucker.

Grants of Plan-Based Awards

The Tile Shop did not grant any plan-based awards during the fiscal year ending December 31, 2011.

Outstanding Equity Awards at Fiscal-Year End

The Tile Shop did not have any outstanding equity awards as of December 31, 2011.

Options Exercises and Stock Vested

None of The Tile Shop's named executive officers exercised options or had equity awards vest during the fiscal year ending December 31, 2011.

Pension Benefits

The Tile Shop did not sponsor any defined benefit pension or other actuarial plan for its named executive officers during the year ended December 31, 2011.

Nonqualified Deferred Compensation

During the fiscal year ended December 31, 2011, The Tile Shop maintained the Deferred Compensation Plan as a deferred compensation plan for its named executive officers, other than Mr. Rucker.

For a further description of the Deferred Compensation Plan, see "Executive Compensation — Compensation Discussion and Analysis — Executive Compensation Program Components — Equity and Equity-Linked Incentives" beginning on page 58 of this prospectus. For a quantitative estimate of the payments that would have accrued to each of our named executive officers under the Deferred Compensation Plan had The Tile Shop undergone a change of control on December 31, 2011, which estimated payments represent the total value the phantom equity units held by each named

executive officer as of December 31, 2011, see “Executive Compensation — Potential Payments Upon Termination or Change of Control” beginning on page 66 of this prospectus.

Potential Payments Upon Termination or Change of Control

The following table sets forth quantitative estimates of the payments and benefits that would have accrued to each of our named executive officers if his employment had been terminated by The Tile Shop or if The Tile Shop had undergone a change of control on December 31, 2011, as described above under “Executive Compensation — Compensation Discussion and Analysis — Executive Compensation Program Components — Equity and Equity-Linked Incentives” above.

Name of Executive Officer	Termination for Cause \$(2)(3)	Termination other than for Cause, Disability, or Death \$(2)(3)	Termination for Disability \$(2)(3)	Termination for Death \$(2)(3)	Change of Control \$(2)
Robert A. Rucker (1)	-	-	-	-	-
Joseph Kinder (1)	-	1,659,600	1,659,000	1,659,000	1,659,000
Carl Randazzo (1)	-	1,659,000	1,659,000	1,659,000	1,659,000
Leigh M. Behrman (1)	-	652,900	652,900	652,900	652,900

(1) These amounts do not take into account any amounts to which the applicable named executive officers would be entitled pursuant to the terms of their respective offer letter agreements, entered into in June 2012.

(2) These amounts were calculated using a fair market value of \$7.732 for The Tile Shop’s Common Units, established by The Tile Shop’s board of managers based on The Tile Shop’s audited financial statements for the fiscal year ended December 31, 2011.

(3) These amounts would be payable to the applicable named executive officer on the tenth or fifteenth anniversary of the date of grant of the applicable award. 100,000 phantom equity units were granted to each of Messrs. Kinder, Randazzo, and Behrman on June 15, 2006 and an additional 100,000 phantom equity units were granted to each of

Messrs. Kinder and Randazzo on each of May 25, 2007 and January 1, 2009.

Offer Letter Agreements

In June 2012, as the result of arm's length negotiations, we entered into an offer letter agreement with Mr. Rucker setting forth the terms and conditions of his employment effective upon consummation of the Business Combination. The offer letter agreement provides for an annual base salary of \$303,991 for the remainder of the 2012 fiscal year and an annual base salary of \$500,000 for the 2013 fiscal year, subject to increases and modifications as determined by our board of directors and its compensation committee. Mr. Rucker's current base salary is \$303,991. Pursuant to the offer letter agreement, Mr. Rucker is entitled to receive severance benefits if his employment is terminated by us without cause at any time or if he is constructively terminated by us, subject to execution of a full release in our favor. In such an event, Mr. Rucker is entitled to continued payment of his base salary for twelve months and an additional payment in an amount equal to twelve times our contribution amount for the monthly health insurance premium for him during the month immediately prior to termination. Upon a change of control, Mr. Rucker is also entitled to full vesting acceleration with respect to any unvested equity awards if he is terminated without cause or if he is constructively terminated prior to the first anniversary of the change of control.

In June 2012, as the result of arm's length negotiations, we entered into offer letter agreements with each of Messrs. Kinder, Randazzo, and Behrman setting forth the terms and conditions of each such individual's respective employment effective upon consummation of the Business Combination. The offer letter agreements provide for an annual base salaries of \$200,000, \$200,000, and \$119,000, respectively, for Messrs. Kinder, Randazzo, and Behrman, subject to increases and modifications as determined by our board of directors and its compensation committee. Messrs. Kinder's, Randazzo's, and Behrman's current base salaries are \$200,000, \$200,000, and \$119,000, respectively. Pursuant to the offer letter agreements, each of Messrs. Kinder, Randazzo and Behrman is entitled to receive severance benefits if his employment is terminated by us without cause at any time or if he is constructively terminated by us, subject to execution of a full release in our favor. In such an event, each of Messrs. Kinder, Randazzo and Behrman is entitled to continued payment of his base salary for six months and an additional payment in an amount equal to six times our contribution amount for the monthly health insurance premium for him during the month immediately prior to termination. Upon a change of control, each of Messrs. Kinder, Randazzo and Behrman is also entitled to full vesting acceleration with respect to any unvested equity awards if he is terminated without cause or if he is constructively terminated prior to the first anniversary of the change of control.

In July 2012, as the result of arm's length negotiations, we entered into an offer letter agreement with Mr. Clayton setting forth the terms and conditions of his employment, effective upon consummation of the Business Combination. The offer letter agreement provides for an annual base salary of \$200,000, subject to increases and modifications as determined by our board of directors and its compensation committee. Mr. Clayton's current base salary is \$200,000. Pursuant to the offer letter agreement, Mr. Clayton is entitled to receive severance benefits if his employment is terminated by us without cause at any time or if he is constructively terminated by us, subject to execution of a full release in our favor. In such an event, Mr. Clayton is entitled to continued payment of his base salary for six months and an additional payment in an amount equal to six times our contribution amount for the monthly health insurance premium for him during the month immediately prior to termination. Upon a change of control, Mr. Clayton is also entitled to full vesting acceleration with respect to any unvested equity awards if he is terminated without cause or if he is constructively terminated prior to the first anniversary of the change of control.

In connection with their offer letter agreements, each of Messrs. Rucker, Clayton, Kinder, Randazzo, and Behrman agreed not to compete, directly or indirectly, with us or solicit any of our employees or business contacts during the term of his employment and for a period of two years, one year, one year, one year, and one year thereafter, respectively. Notwithstanding the foregoing, we may, at our election, extend the term of the non-compete and non-solicit obligations to which Messrs. Clayton, Kinder, and Randazzo are subject to be for a period of two years following termination of employment; provided, that we provide the applicable individual with continued payment of his base salary for twelve months (in lieu of six months) and an additional payment in an amount equal to twelve times (in lieu of six times) our contribution amount for the monthly health insurance premium for him during the month immediately prior to termination.

Limitation on Liability and Indemnification Matters

Our certificate of incorporation and bylaws provide that we will indemnify our directors and officers, and may indemnify our employees and other agents, to the fullest extent permitted by the Delaware General Corporation Law, which prohibits our certificate of incorporation from limiting the liability of our directors for the following:

- any breach of the director's duty of loyalty to us or to our stockholders;
- acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law;
- unlawful payment of dividends or unlawful stock repurchases or redemptions; and
- any transaction from which the director derived an improper personal benefit.

If Delaware law is amended to authorize corporate action further eliminating or limiting the personal liability of a director, then the liability of our directors will be eliminated or limited to the fullest extent permitted by Delaware law, as so amended. Our certificate of incorporation does not eliminate a director's duty of care and, in appropriate circumstances, equitable remedies, such as injunctive or other forms of non-monetary relief, remain available under Delaware law. This provision also does not affect a director's responsibilities under any other laws, such as the federal sec