

Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

Stone Harbor Emerging Markets Income Fund  
Form 40-17G  
February 13, 2012  
February 13, 2012

U.S. Securities and Exchange Commission

100 F Street N.E.

Washington, DC 20549

Re: Stone Harbor Emerging Markets Income Fund  
Investment Company Act of 1940-Rule 17g-1(g)  
Bonding of Officers and Employees  
(Stone Harbor Emerging Markets Income Fund File No. 811-22473)

Dear Sir or Madam:

Pursuant to Rule 17g-1(g)(1) under the Investment Company Act of 1940, as amended ( 1940 Act), enclosed please find a copy of the financial institution bond (the Bond ) in favor of Stone Harbor Emerging Markets Income Fund, a management investment company registered under the 1940 Act, and resolutions relating to the Bond.

The term of the Bond is December 22, 2011 through December 22, 2012, and the premium for the Bond has been paid through December 22, 2012. The Bond provides fidelity coverage with a \$1,000,000 liability limit.

Please call me at (303) 623-2577 if you have any questions.

Sincerely,

/s/ JoEllen L. Legg  
*JoEllen L. Legg*  
Assistant Secretary  
Stone Harbor Emerging Markets Income Fund  
Enclosures

**Chubb Group of Insurance Companies**

15 Mountain View Road, Warren, New Jersey 07059

NAME OF ASSURED (including its **Subsidiaries**):

STONE HARBOR EMERGING MARKETS INCOME FUND

1290 BROADWAY SUITE 1100  
DENVER, COLO 80203

**DECLARATIONS  
FINANCIAL INSTITUTION INVESTMENT  
COMPANY ASSET PROTECTION BOND**

Bond Number: 82302678

**FEDERAL INSURANCE COMPANY**

Incorporated under the laws of Indiana  
a stock insurance company herein called the COMPANY  
Capital Center, 251 North Illinois, Suite 1100  
Indianapolis, IN 46204-1927

**ITEM 1. BOND PERIOD:** from 12:01 a.m. on December 22, 2011  
to 12:01 a.m. on December 22, 2012

**ITEM 2. LIMITS OF LIABILITY--DEDUCTIBLE AMOUNTS:**

If Not Covered is inserted below opposite any specified INSURING CLAUSE, such INSURING CLAUSE and any other reference shall be deemed to be deleted. **There shall be no deductible applicable to any loss under INSURING CLAUSE 1. sustained by any Investment Company.**

INSURING CLAUSE	LIMIT OF LIABILITY	DEDUCTIBLE AMOUNT
1. Employee	\$ 1,000,000	\$ 0
2. On Premises	\$ 1,000,000	\$ 10,000
3. In Transit	\$ 1,000,000	\$ 10,000
4. Forgery or Alteration	\$ 1,000,000	\$ 10,000
5. Extended Forgery	\$ 1,000,000	\$ 10,000
6. Counterfeit Money	\$ 1,000,000	\$ 10,000
7. Threats to Person	\$ 1,000,000	\$ 10,000
8. Computer System	\$ 1,000,000	\$ 10,000
9. Voice Initiated Funds Transfer Instruction	\$ 1,000,000	\$ 10,000
10. Uncollectible Items of Deposit	\$ 1,000,000	\$ 10,000
11. Audit Expense	\$ 25,000	\$ 0

**ITEM 3. THE LIABILITY OF THE COMPANY IS ALSO SUBJECT TO THE TERMS OF THE FOLLOWING ENDORSEMENTS EXECUTED SIMULTANEOUSLY HEREWITH:**

1-3

**IN WITNESS WHEREOF, THE COMPANY** has caused this Bond to be signed by its authorized officers, but it shall not be valid unless also signed by an authorized representative of the Company.

ICAP Bond (5-98) - Federal

Form 17-02-1421 (Ed. 5-98) Page 1 of 1

The COMPANY, in consideration of payment of the required premium, and in reliance on the APPLICATION and all other statements made and information furnished to the COMPANY by the ASSURED, and subject to the DECLARATIONS made a part of this Bond and to all other terms and conditions of this Bond, agrees to pay the ASSURED for:

*Insuring Clauses*

*Employee*

1. Loss resulting directly from **Larceny** or **Embezzlement** committed by any **Employee**, alone or in collusion with others.

*On Premises*

2. Loss of **Property** resulting directly from robbery, burglary, false pretenses, common law or statutory larceny, misplacement, mysterious unexplainable disappearance, damage, destruction or removal, from the possession, custody or control of the ASSURED, while such **Property** is lodged or deposited at premises located anywhere.

*In Transit*

3. Loss of **Property** resulting directly from common law or statutory larceny, misplacement, mysterious unexplainable disappearance, damage or destruction, while the **Property** is in transit anywhere:
  - a. in an armored motor vehicle, including loading and unloading thereof,
  - b. in the custody of a natural person acting as a messenger of the ASSURED, or
  - c. in the custody of a **Transportation Company** and being transported in a conveyance other than an armored motor vehicle provided, however, that covered **Property** transported in such manner is limited to the following:
    - (1) written records,
    - (2) securities issued in registered form, which are not endorsed or are restrictively endorsed, or
    - (3) negotiable instruments not payable to bearer, which are not endorsed or are restrictively endorsed.

Coverage under this INSURING CLAUSE begins immediately on the receipt of such **Property** by the natural person or **Transportation Company** and ends immediately on delivery to the premises of the addressee or to any representative of the addressee located anywhere.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 1 of 19

**Insuring Clauses**  
(continued)

*Forgery Or Alteration*

4. Loss resulting directly from:
- a. **Forgery** on, or fraudulent material alteration of, any bills of exchange, checks, drafts, acceptances, certificates of deposits, promissory notes, due bills, money orders, orders upon public treasuries, letters of credit, other written promises, orders or directions to pay sums certain in money, or receipts for the withdrawal of **Property**, or
  - b. transferring, paying or delivering any funds or other **Property**, or establishing any credit or giving any value in reliance on any written instructions, advices or applications directed to the ASSURED authorizing or acknowledging the transfer, payment, delivery or receipt of funds or other **Property**, which instructions, advices or applications fraudulently purport to bear the handwritten signature of any customer of the ASSURED, or shareholder or subscriber to shares of an **Investment Company**, or of any financial institution or **Employee** but which instructions, advices or applications either bear a **Forgery** or have been fraudulently materially altered without the knowledge and consent of such customer, shareholder, subscriber, financial institution or **Employee**;

excluding, however, under this INSURING CLAUSE any loss covered under INSURING CLAUSE 5. of this Bond, whether or not coverage for INSURING CLAUSE 5. is provided for in the DECLARATIONS of this Bond.

For the purpose of this INSURING CLAUSE, a mechanically reproduced facsimile signature is treated the same as a handwritten signature.

*Extended Forgery*

5. Loss resulting directly from the ASSURED having, in good faith, and in the ordinary course of business, for its own account or the account of others in any capacity:
- a. acquired, accepted or received, accepted or received, sold or delivered, or given value, extended credit or assumed liability, in reliance on any original **Securities, documents or other written instruments** which prove to:
    - (1) bear a **Forgery** or a fraudulently material alteration,
    - (2) have been lost or stolen, or
    - (3) be **Counterfeit**, or
  - b. guaranteed in writing or witnessed any signatures on any transfer, assignment, bill of sale, power of attorney, guarantee, endorsement or other obligation upon or in connection with any **Securities, documents or other written instruments**.

Actual physical possession, and continued actual physical possession if taken as collateral, of such **Securities, documents or other written instruments** by an **Employee, Custodian**, or a Federal or State chartered deposit institution of the ASSURED is a condition precedent to the ASSURED having relied on such items. Release or return of such collateral is an acknowledgment by the ASSURED that it no longer relies on such collateral.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 2 of 19

**Insuring Clauses**

*Extended Forgery*

*(continued)*

For the purpose of this INSURING CLAUSE, a mechanically reproduced facsimile signature is treated the same as a handwritten signature.

*Counterfeit Money*

6. Loss resulting directly from the receipt by the ASSURED in good faith of any **Counterfeit** money.

*Threats To Person*

7. Loss resulting directly from surrender of **Property** away from an office of the ASSURED as a result of a threat communicated to the ASSURED to do bodily harm to an **Employee** as defined in Section 1.e. (1), (2) and (5), a **Relative** or invitee of such **Employee**, or a resident of the household of such **Employee**, who is, or allegedly is, being held captive provided, however, that prior to the surrender of such **Property**:

a. the **Employee** who receives the threat has made a reasonable effort to notify an officer of the ASSURED who is not involved in such threat, and

b. the ASSURED has made a reasonable effort to notify the Federal Bureau of Investigation and local law enforcement authorities concerning such threat.

It is agreed that for purposes of this INSURING CLAUSE, any **Employee** of the ASSURED, as set forth in the preceding paragraph, shall be deemed to be an ASSURED hereunder, but only with respect to the surrender of money, securities and other tangible personal property in which such **Employee** has a legal or equitable interest.

*Computer System*

8. Loss resulting directly from fraudulent:

a. entries of data into, or

b. changes of data elements or programs within,

a **Computer System**, provided the fraudulent entry or change causes:

(1) funds or other property to be transferred, paid or delivered,

(2) an account of the ASSURED or of its customer to be added, deleted, debited or credited, or

(3) an unauthorized account or a fictitious account to be debited or credited.



**Insuring Clauses**

(continued)

*Voice Initiated Funds*

*Transfer Instruction*

9. Loss resulting directly from **Voice Initiated Funds Transfer Instruction** directed to the ASSURED authorizing the transfer of dividends or redemption proceeds of **Investment Company** shares from a **Customer**'s account, provided such **Voice Initiated Funds Transfer Instruction** was:

- a. received at the ASSURED'S offices by those **Employees** of the ASSURED specifically authorized to receive the **Voice Initiated Funds Transfer Instruction**,
- b. made by a person purporting to be a **Customer**, and
- c. made by said person for the purpose of causing the ASSURED or **Customer** to sustain a loss or making an improper personal financial gain for such person or any other person.

In order for coverage to apply under this INSURING CLAUSE, all **Voice Initiated Funds Transfer Instructions** must be received and processed in accordance with the Designated Procedures outlined in the APPLICATION furnished to the COMPANY.

*Uncollectible Items of*

*Deposit*

10. Loss resulting directly from the ASSURED having credited an account of a customer, shareholder or subscriber on the faith of any **Items of Deposit** which prove to be uncollectible, provided that the crediting of such account causes:

- a. redemptions or withdrawals to be permitted,
- b. shares to be issued, or
- c. dividends to be paid,

from an account of an **Investment Company**.

In order for coverage to apply under this INSURING CLAUSE, the ASSURED must hold **Items of Deposit** for the minimum number of days stated in the APPLICATION before permitting any redemptions or withdrawals, issuing any shares or paying any dividends with respect to such **Items of Deposit**.

**Items of Deposit** shall not be deemed uncollectible until the ASSURED'S standard collection procedures have failed.

*Audit Expense*

Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

11. Expense incurred by the ASSURED for that part of the cost of audits or examinations required by any governmental regulatory authority or self-regulatory organization to be conducted by such authority, organization or their appointee by reason of the discovery of loss sustained by the ASSURED and covered by this Bond.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 4 of 19



**General Agreements**

*Additional Companies*

*Included As Assured*

A. If more than one corporation, or **Investment Company**, or any combination of them is included as the ASSURED herein:

(1) The total liability of the COMPANY under this Bond for loss or losses sustained by any one or more or all of them shall not exceed the limit for which the COMPANY would be liable under this Bond if all such loss were sustained by any one of them.

(2) Only the first named ASSURED shall be deemed to be the sole agent of the others for all purposes under this Bond, including but not limited to the giving or receiving of any notice or proof required to be given and for the purpose of effecting or accepting any amendments to or termination of this Bond. The COMPANY shall furnish each **Investment Company** with a copy of the Bond and with any amendment thereto, together with a copy of each formal filing of claim by any other named ASSURED and notification of the terms of the settlement of each such claim prior to the execution of such settlement.

(3) The COMPANY shall not be responsible for the proper application of any payment made hereunder to the first named ASSURED.

(4) Knowledge possessed or discovery made by any partner, director, trustee, officer or supervisory employee of any ASSURED shall constitute knowledge or discovery by all the ASSUREDS for the purposes of this Bond.

(5) If the first named ASSURED ceases for any reason to be covered under this Bond, then the ASSURED next named on the APPLICATION shall thereafter be considered as the first named ASSURED for the purposes of this Bond.

*Representation Made By*

*Assured*

B. The ASSURED represents that all information it has furnished in the APPLICATION for this Bond or otherwise is complete, true and correct. Such APPLICATION and other information constitute part of this Bond.

The ASSURED must promptly notify the COMPANY of any change in any fact or circumstance which materially affects the risk assumed by the COMPANY under this Bond.

Any intentional misrepresentation, omission, concealment or incorrect statement of a material fact, in the APPLICATION or otherwise, shall be grounds for rescission of this Bond.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 5 of 19

**General Agreements**

*(continued)*

*Additional Offices Or*

*Employees - Consolidation,*

*Merger Or Purchase Or*

*Acquisition Of Assets Or  
Liabilities - Notice To*

*Company*

C. If the ASSURED, other than an **Investment Company**, while this Bond is in force, merges or consolidates with, or purchases or acquires assets or liabilities of another institution, the ASSURED shall not have the coverage afforded under this Bond for loss which has:

(1) occurred or will occur on premises, or

(2) been caused or will be caused by an employee, or

(3) arisen or will arise out of the assets or liabilities, of such institution, unless the ASSURED:

a. gives the COMPANY written notice of the proposed consolidation, merger or purchase or acquisition of assets or liabilities prior to the proposed effective date of such action, and

b. obtains the written consent of the COMPANY to extend some or all of the coverage provided by this Bond to such additional exposure, and

c. on obtaining such consent, pays to the COMPANY an additional premium.

*Change Of Control -*

*Notice To Company*

D. When the ASSURED learns of a change in control (other than in an **Investment Company**), as set forth in Section 2(a) (9) of the Investment Company Act of 1940, the ASSURED shall within sixty (60) days give written notice to the COMPANY setting forth:

(1) the names of the transferors and transferees (or the names of the beneficial owners if the voting securities are registered in another name),

(2) the total number of voting securities owned by the transferors and the transferees (or the beneficial owners), both immediately before and after the transfer, and

(3) the total number of outstanding voting securities. Failure to give the required notice shall result in termination of coverage for any loss involving a transferee, to be effective on the date of such change in control.

*Court Costs And*

*Attorneys Fees*

E. The COMPANY will indemnify the ASSURED for court costs and reasonable attorneys fees incurred and paid by the ASSURED in defense, whether or not successful, whether or not fully litigated on the merits and whether or not settled, of any claim, suit or legal proceeding with respect to which the ASSURED would be entitled to recovery under this Bond. However, with respect to INSURING CLAUSE 1., this Section shall only apply in the event that:

(1) an **Employee** admits to being guilty of **Larceny or Embezzlement**,

(2) an **Employee** is adjudicated to be guilty of **Larceny or Embezzlement**, or

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 6 of 19

**General Agreements**

*Court Costs And*

*Attorneys Fees*

*(continued)*

(3) in the absence of 1 or 2 above, an arbitration panel agrees, after a review of an agreed statement of facts between the COMPANY and the ASSURED, that an **Employee** would be found guilty of **Larceny or Embezzlement** if such **Employee** were prosecuted.

The ASSURED shall promptly give notice to the COMPANY of any such suit or legal proceeding and at the request of the COMPANY shall furnish copies of all pleadings and pertinent papers to the COMPANY. The COMPANY may, at its sole option, elect to conduct the defense of all or part of such legal proceeding. The defense by the COMPANY shall be in the name of the ASSURED through attorneys selected by the COMPANY. The ASSURED shall provide all reasonable information and assistance as required by the COMPANY for such defense.

If the COMPANY declines to defend the ASSURED, no settlement without the prior written consent of the COMPANY nor judgment against the ASSURED shall determine the existence, extent or amount of coverage under this Bond.

If the amount demanded in any such suit or legal proceeding is within the DEDUCTIBLE AMOUNT, if any, the COMPANY shall have no liability for court costs and attorney's fees incurred in defending all or part of such suit or legal proceeding.

If the amount demanded in any such suit or legal proceeding is in excess of the LIMIT OF LIABILITY stated in ITEM 2. of the DECLARATIONS for the applicable INSURING CLAUSE, the COMPANY'S liability for court costs and attorney's fees incurred in defending all or part of such suit or legal proceedings is limited to the proportion of such court costs and attorney's fees incurred that the LIMIT OF LIABILITY stated in ITEM 2. of the DECLARATIONS for the applicable INSURING CLAUSE bears to the total of the amount demanded in such suit or legal proceeding.

If the amount demanded in any such suit or legal proceeding is in excess of the DEDUCTIBLE AMOUNT, if any, but within the LIMIT OF LIABILITY stated in ITEM 2. of the DECLARATIONS for the applicable INSURING CLAUSE, the COMPANY'S liability for court costs and attorney's fees incurred in defending all or part of such suit or legal proceedings shall be limited to the proportion of such court costs or attorney's fees that the amount demanded that would be payable under this Bond after application of the DEDUCTIBLE AMOUNT, bears to the total amount demanded.

Amounts paid by the COMPANY for court costs and attorney's fees shall be in addition to the LIMIT OF LIABILITY stated in ITEM 2. of the DECLARATIONS.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 7 of 19

*Conditions And*

*Limitations*

*Definitions*

1. As used in this Bond:
  - a. **Computer System** means a computer and all input, output, processing, storage, off-line media libraries, and communication facilities which are connected to the computer and which are under the control and supervision of the operating system(s) or application(s) software used by the ASSURED.
  - b. **Counterfeit** means an imitation of an actual valid original which is intended to deceive and be taken as the original.
  - c. **Custodian** means the institution designated by an **Investment Company** to maintain possession and control of its assets.
  - d. **Customer** means an individual, corporate, partnership, trust customer, shareholder or subscriber of an **Investment Company** which has a written agreement with the ASSURED for **Voice Initiated Funds Transfer Instruction**.
  - e. **Employee** means:
    - (1) an officer of the ASSURED,
    - (2) a natural person while in the regular service of the ASSURED at any of the ASSURED S premises and compensated directly by the ASSURED through its payroll system and subject to the United States Internal Revenue Service Form W-2 or equivalent income reporting plans of other countries, and whom the ASSURED has the right to control and direct both as to the result to be accomplished and details and means by which such result is accomplished in the performance of such service,
    - (3) a guest student pursuing studies or performing duties in any of the ASSURED S premises,
    - (4) an attorney retained by the ASSURED and an employee of such attorney while either is performing legal services for the ASSURED,
    - (5) a natural person provided by an employment contractor to perform employee duties for the ASSURED under the ASSURED S supervision at any of the ASSURED S premises,
    - (6) an employee of an institution merged or consolidated with the ASSURED prior to the effective date of this Bond,
    - (7) a director or trustee of the ASSURED, but only while performing acts within the scope of the customary and usual duties of any officer or other employee of the ASSURED or while acting as a member of any committee duly elected or appointed to examine or audit or have custody of or access to **Property** of the ASSURED, or

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 8 of 19

**Conditions And**

**Limitations**

**Definitions**

*(continued)*

(8) each natural person, partnership or corporation authorized by written agreement with the ASSURED to perform services as electronic data processor of checks or other accounting records related to such checks but only while such person, partnership or corporation is actually performing such services and not:

- a. creating, preparing, modifying or maintaining the ASSURED S computer software or programs, or
- b. acting as transfer agent or in any other agency capacity in issuing checks, drafts or securities for the ASSURED,

(9) any partner, officer or employee of an investment advisor, an underwriter (distributor), a transfer agent or shareholder accounting recordkeeper, or an administrator, for an **Investment Company** while performing acts coming within the scope of the customary and usual duties of an officer or employee of an **Investment Company** or acting as a member of any committee duly elected or appointed to examine, audit or have custody of or access to **Property of an Investment Company**.

The term **Employee** shall not include any partner, officer or employee of a transfer agent, shareholder accounting recordkeeper or administrator:

- a. which is not an affiliated person (as defined in Section 2(a) of the Investment Company Act of 1940) of an **Investment Company** or of the investment advisor or underwriter (distributor) of such **Investment Company**, or
- b. which is a bank (as defined in Section 2(a) of the Investment Company Act of 1940).

This Bond does not afford coverage in favor of the employers of persons as set forth in e. (4), (5) and (8) above, and upon payment to the ASSURED by the COMPANY resulting directly from **Larceny or Embezzlement** committed by any of the partners, officers or employees of such employers, whether acting alone or in collusion with others, an assignment of such of the ASSURED S rights and causes of action as it may have against such employers by reason of such acts so committed shall, to the extent of such payment, be given by the ASSURED to the COMPANY, and the ASSURED shall execute all papers necessary to secure to the COMPANY the rights provided for herein.

Each employer of persons as set forth in e.(4), (5) and (8) above and the partners, officers and other employees of such employers shall collectively be deemed to be one person for all the purposes of this Bond; excepting, however, the fifth paragraph of Section 13.

Independent contractors not specified in e.(4), (5) or (8) above, intermediaries, agents, brokers or other representatives of the same general character shall not be considered **Employees**.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 9 of 19

**Conditions And**

**Limitations**

**Definitions**

(continued)

f. **Forgery** means the signing of the name of another natural person with the intent to deceive but does not mean a signature which consists in whole or in part of one's own name, with or without authority, in any capacity for any purpose.

g. **Investment Company** means any investment company registered under the Investment Company Act of 1940 and listed under the NAME OF ASSURED on the DECLARATIONS.

h. **Items of Deposit** means one or more checks or drafts drawn upon a financial institution in the United States of America.

i. **Larceny or Embezzlement** means larceny or embezzlement as defined in Section 37 of the Investment Company Act of 1940.

j. **Property** means money, revenue and other stamps; securities; including any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of deposit, certificate of interest or participation in any profit-sharing agreement, collateral trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any interest or instruments commonly known as a security under the Investment Company Act of 1940, any other certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase any of the foregoing; bills of exchange; acceptances; checks; withdrawal orders; money orders; travelers' letters of credit; bills of lading; abstracts of title; insurance policies, deeds, mortgages on real estate and/or upon chattels and interests therein; assignments of such policies, deeds or mortgages; other valuable papers, including books of accounts and other records used by the ASSURED in the conduct of its business (but excluding all electronic data processing records); and, all other instruments similar to or in the nature of the foregoing in which the ASSURED acquired an interest at the time of the ASSURED'S consolidation or merger with, or purchase of the principal assets of, a predecessor or which are held by the ASSURED for any purpose or in any capacity and whether so held gratuitously or not and whether or not the ASSURED is liable therefor.

k. **Relative** means the spouse of an **Employee** or partner of the ASSURED and any unmarried child supported wholly by, or living in the home of, such **Employee** or partner and being related to them by blood, marriage or legal guardianship.

l. **Securities, documents or other written instruments** means original (including original counterparts) negotiable or non-negotiable instruments, or assignments thereof, which in and of themselves represent an equitable interest, ownership, or debt and which are in the ordinary course of business transferable by delivery of such instruments with any necessary endorsements or assignments.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 10 of 19

**Conditions And**

**Limitations**

**Definitions**

*(continued)*

m. **Subsidiary** means any organization that, at the inception date of this Bond, is named in the APPLICATION or is created during the BOND PERIOD and of which more than fifty percent (50%) of the outstanding securities or voting rights representing the present right to vote for election of directors is owned or controlled by the ASSURED either directly or through one or more of its subsidiaries.

n. **Transportation Company** means any organization which provides its own or its leased vehicles for transportation or which provides freight forwarding or air express services.

o. **Voice Initiated Election** means any election concerning dividend options available to **Investment Company** shareholders or subscribers which is requested by voice over the telephone.

p. **Voice Initiated Redemption** means any redemption of shares issued by an **Investment Company** which is requested by voice over the telephone.

q. **Voice Initiated Funds Transfer Instruction** means any **Voice Initiated Redemption** or **Voice Initiated Election**.

For the purposes of these definitions, the singular includes the plural and the plural includes the singular, unless otherwise indicated.

**General Exclusions -  
Applicable to All Insuring**

2. **This bond does not directly or indirectly cover:**

**Clauses**

a. loss not reported to the COMPANY in writing within sixty (60) days after termination of this Bond as an entirety;

b. loss due to riot or civil commotion outside the United States of America and Canada, or any loss due to military, naval or usurped power, war or insurrection. This Section 2.b., however, shall not apply to loss which occurs in transit in the circumstances recited in INSURING CLAUSE 3., provided that when such transit was initiated there was no knowledge on the part of any person acting for the ASSURED of such riot, civil commotion, military, naval or usurped power, war or insurrection;

c. loss resulting from the effects of nuclear fission or fusion or radioactivity;

d. loss of potential income including, but not limited to, interest and dividends not realized by the ASSURED or by any customer of the ASSURED;

e. damages of any type for which the ASSURED is legally liable, except compensatory damages, but not multiples thereof, arising from a loss covered under this Bond;

f. costs, fees and expenses incurred by the ASSURED in establishing the existence of or amount of loss under this Bond, except to the extent covered under INSURING CLAUSE 11.;

g. loss resulting from indirect or consequential loss of any nature;

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 11 of 19



**Conditions And**

**Limitations**

*General Exclusions -*

*Applicable to All Insuring*

*Clauses*

*(continued)*

- h. loss resulting from dishonest acts by any member of the Board of Directors or Board of Trustees of the ASSURED who is not an **Employee**, acting alone or in collusion with others;
- i. loss, or that part of any loss, resulting solely from any violation by the ASSURED or by any **Employee**:
  - (1) of any law regulating:
    - a. the issuance, purchase or sale of securities,
    - b. securities transactions on security or commodity exchanges or the over the counter market,
    - c. investment companies,
    - d. investment advisors, or
  - (2) of any rule or regulation made pursuant to any such law; or
- j. loss of confidential information, material or data;
- k. loss resulting from voice requests or instructions received over the telephone, provided however, this Section 2.k. shall not apply to INSURING CLAUSE 7. or 9.

*Specific Exclusions -*

*Applicable To All Insuring*

*Clauses Except Insuring*

*Clause 1.*

3. **This Bond does not directly or indirectly cover:**

- a. loss caused by an **Employee**, provided, however, this Section 3.a. shall not apply to loss covered under INSURING CLAUSE 2. or 3. which results directly from misplacement, mysterious unexplainable disappearance, or damage or destruction of **Property**;
- b. loss through the surrender of property away from premises of the ASSURED as a result of a threat:
  - (1) to do bodily harm to any natural person, except loss of **Property** in transit in the custody of any person acting as messenger of the ASSURED, provided that when such transit was initiated there was no knowledge by the ASSURED of any such threat, and provided further that this Section 3.b. shall not apply to INSURING CLAUSE 7., or
  - (2) to do damage to the premises or **Property** of the ASSURED;
- c. loss resulting from payments made or withdrawals from any account involving erroneous credits to such account;
- d. loss involving **Items of Deposit** which are not finally paid for any reason provided however, that this Section 3.d. shall not apply to INSURING CLAUSE 10.;
- e. loss of property while in the mail;

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 12 of 19

**Conditions And**

**Limitations**

*Specific Exclusions -*

*Applicable To All Insuring*

*Clauses Except Insuring*

*Clause 1.*

*(continued)*

f. loss resulting from the failure for any reason of a financial or depository institution, its receiver or other liquidator to pay or deliver funds or other **Property** to the ASSURED provided further that this Section 3.f. shall not apply to loss of **Property** resulting directly from robbery, burglary, misplacement, mysterious unexplainable disappearance, damage, destruction or removal from the possession, custody or control of the ASSURED.

g. loss of **Property** while in the custody of a **Transportation Company**, provided however, that this Section 3.g. shall not apply to INSURING CLAUSE 3.;

h. loss resulting from entries or changes made by a natural person with authorized access to a **Computer System** who acts in good faith on instructions, unless such instructions are given to that person by a software contractor or its partner, officer, or employee authorized by the ASSURED to design, develop, prepare, supply, service, write or implement programs for the ASSURED's **Computer System**; or

i. loss resulting directly or indirectly from the input of data into a **Computer System** terminal, either on the premises of the customer of the ASSURED or under the control of such a customer, by a customer or other person who had authorized access to the customer's authentication mechanism.

*Specific Exclusions -*

*Applicable To All Insuring*

*Clauses Except Insuring*

*Clauses 1., 4., And 5.*

4. **This bond does not directly or indirectly cover:**

a. loss resulting from the complete or partial non-payment of or default on any loan whether such loan was procured in good faith or through trick, artifice, fraud or false pretenses; provided, however, this Section 4.a. shall not apply to INSURING CLAUSE 8.;

b. loss resulting from forgery or any alteration;

c. loss involving a counterfeit provided, however, this Section 4.c. shall not apply to INSURING CLAUSE 5. or 6.

*Limit Of Liability/Non-*

*Reduction And Non-*

*Accumulation Of Liability*

5. At all times prior to termination of this Bond, this Bond shall continue in force for the limit stated in the applicable sections of ITEM 2. of the DECLARATIONS, notwithstanding any previous loss for which the COMPANY may have paid or be liable to pay under this Bond provided, however, that the liability of the COMPANY under this Bond with respect to all loss resulting from:

Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

- a. any one act of burglary, robbery or hold-up, or attempt thereat, in which no **Employee** is concerned or implicated, or
  
- b. any one unintentional or negligent act on the part of any one person resulting in damage to or destruction or misplacement of **Property**, or
  
- c. all acts, other than those specified in a. above, of any one person, or

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 13 of 19

**Conditions And**

**Limitations**

*Limit Of Liability/Non-*

*Reduction And Non-*

*Accumulation Of Liability*

*(continued)*

d. any one casualty or event other than those specified in a., b., or c. above, shall be deemed to be one loss and shall be limited to the applicable LIMIT OF LIABILITY stated in ITEM 2. of the DECLARATIONS of this Bond irrespective of the total amount of such loss or losses and shall not be cumulative in amounts from year to year or from period to period.

All acts, as specified in c. above, of any one person which

- i. directly or indirectly aid in any way wrongful acts of any other person or persons, or
- ii. permit the continuation of wrongful acts of any other person or persons

whether such acts are committed with or without the knowledge of the wrongful acts of the person so aided, and whether such acts are committed with or without the intent to aid such other person, shall be deemed to be one loss with the wrongful acts of all persons so aided.

*Discovery*

6. This Bond applies only to loss first discovered by an officer of the ASSURED during the BOND PERIOD. Discovery occurs at the earlier of an officer of the ASSURED being aware of:

- a. facts which may subsequently result in a loss of a type covered by this Bond, or
- b. an actual or potential claim in which it is alleged that the ASSURED is liable to a third party,

regardless of when the act or acts causing or contributing to such loss occurred, even though the amount of loss does not exceed the applicable DEDUCTIBLE AMOUNT, or the exact amount or details of loss may not then be known.

*Notice To Company -*

*Proof - Legal Proceedings*

*Against Company*

7. a. The ASSURED shall give the COMPANY notice thereof at the earliest practicable moment, not to exceed sixty (60) days after discovery of loss, in an amount that is in excess of 50% of the applicable DEDUCTIBLE AMOUNT, as stated in ITEM 2. of the DECLARATIONS.

b. The ASSURED shall furnish to the COMPANY proof of loss, duly sworn to, with full particulars within six (6) months after such discovery.

## Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

- c. Securities listed in a proof of loss shall be identified by certificate or bond numbers, if issued with them.
  
- d. Legal proceedings for the recovery of any loss under this Bond shall not be brought prior to the expiration of sixty (60) days after the proof of loss is filed with the COMPANY or after the expiration of twenty-four (24) months from the discovery of such loss.
  
- e. This Bond affords coverage only in favor of the ASSURED. No claim, suit, action or legal proceedings shall be brought under this Bond by anyone other than the ASSURED.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 14 of 19

**Conditions And**

**Limitations**

*Notice To Company -*

f. Proof of loss involving **Voice Initiated Funds Transfer Instruction** shall include electronic recordings of such instructions.

*Proof - Legal Proceedings*

*Against Company (continued)*

*Deductible Amount*

8. The COMPANY shall not be liable under any INSURING CLAUSES of this Bond on account of loss unless the amount of such loss, after deducting the net amount of all reimbursement and/or recovery obtained or made by the ASSURED, other than from any Bond or policy of insurance issued by an insurance company and covering such loss, or by the COMPANY on account thereof prior to payment by the COMPANY of such loss, shall exceed the DEDUCTIBLE AMOUNT set forth in ITEM 3. of the DECLARATIONS, and then for such excess only, but in no event for more than the applicable LIMITS OF LIABILITY stated in ITEM 2. of the DECLARATIONS.

There shall be no deductible applicable to any loss under INSURING CLAUSE 1. sustained by any **Investment Company**.

*Valuation*

9. BOOKS OF ACCOUNT OR OTHER RECORDS The value of any loss of **Property** consisting of books of account or other records used by the ASSURED in the conduct of its business shall be the amount paid by the ASSURED for blank books, blank pages, or other materials which replace the lost books of account or other records, plus the cost of labor paid by the ASSURED for the actual transcription or copying of data to reproduce such books of account or other records.

The value of any loss of **Property** other than books of account or other records used by the ASSURED in the conduct of its business, for which a claim is made shall be determined by the average market value of such **Property** on the business day immediately preceding discovery of such loss provided, however, that the value of any **Property** replaced by the ASSURED with the consent of the COMPANY and prior to the settlement of any claim for such **Property** shall be the actual market value at the time of replacement.

In the case of a loss of interim certificates, warrants, rights or other securities, the production of which is necessary to the exercise of subscription, conversion, redemption or deposit privileges, the value of them shall be the market value of such privileges immediately preceding their expiration if said loss is not discovered until after their expiration. If no market price is quoted for such **Property** or for such privileges, the value shall be fixed by agreement between the parties.

**OTHER PROPERTY**

The value of any loss of **Property**, other than as stated above, shall be the actual cash value or the cost of repairing or replacing such **Property** with **Property** of like quality and value, whichever is less.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 15 of 19

**Conditions And**

**Limitations**

(continued)

*Securities Settlement*

10. In the event of a loss of securities covered under this Bond, the COMPANY may, at its sole discretion, purchase replacement securities, tender the value of the securities in money, or issue its indemnity to effect replacement securities.

The indemnity required from the ASSURED under the terms of this Section against all loss, cost or expense arising from the replacement of securities by the COMPANY S indemnity shall be:

- a. for securities having a value less than or equal to the applicable DEDUCTIBLE AMOUNT - one hundred (100%) percent;
- b. for securities having a value in excess of the DEDUCTIBLE AMOUNT but within the applicable LIMIT OF LIABILITY - the percentage that the DEDUCTIBLE AMOUNT bears to the value of the securities;
- c. for securities having a value greater than the applicable LIMIT OF LIABILITY - the percentage that the DEDUCTIBLE AMOUNT and portion in excess of the applicable LIMIT OF LIABILITY bears to the value of the securities.

The value referred to in Section 10.a., b., and c. is the value in accordance with Section 9, VALUATION, regardless of the value of such securities at the time the loss under the COMPANY S indemnity is sustained.

The COMPANY is not required to issue its indemnity for any portion of a loss of securities which is not covered by this Bond; however, the COMPANY may do so as a courtesy to the ASSURED and at its sole discretion.

The ASSURED shall pay the proportion of the Company s premium charge for the Company s indemnity as set forth in Section 10.a., b., and c. No portion of the LIMIT OF LIABILITY shall be used as payment of premium for any indemnity purchased by the ASSURED to obtain replacement securities.

*Subrogation - Assignment - Recovery*

11. In the event of a payment under this Bond, the COMPANY shall be subrogated to all of the ASSURED S rights of recovery against any person or entity to the extent of such payment. On request, the ASSURED shall deliver to the COMPANY an assignment of the ASSURED S rights, title and interest and causes of action against any person or entity to the extent of such payment.

Recoveries, whether effected by the COMPANY or by the ASSURED, shall be applied net of the expense of such recovery in the following order:

- a. first, to the satisfaction of the ASSURED S loss which would otherwise have been paid but for the fact that it is in excess of the applicable LIMIT OF LIABILITY,
- b. second, to the COMPANY in satisfaction of amounts paid in settlement of the ASSURED S claim,
- c. third, to the ASSURED in satisfaction of the applicable DEDUCTIBLE AMOUNT, and

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 16 of 19

**Conditions And**

**Limitations**

*Subrogation - Assignment - Recovery*

d. fourth, to the ASSURED in satisfaction of any loss suffered by the ASSURED which was not covered under this Bond.

(continued)

Recovery from reinsurance or indemnity of the COMPANY shall not be deemed a recovery under this section.

*Cooperation Of Assured*

12. At the COMPANY S request and at reasonable times and places designated by the COMPANY, the ASSURED shall:

- a. submit to examination by the COMPANY and subscribe to the same under oath,
- b. produce for the COMPANY S examination all pertinent records, and
- c. cooperate with the COMPANY in all matters pertaining to the loss.

The ASSURED shall execute all papers and render assistance to secure to the COMPANY the rights and causes of action provided for under this Bond. The ASSURED shall do nothing after loss to prejudice such rights or causes of action.

*Termination*

13. If the Bond is for a sole ASSURED, it shall not be terminated unless written notice shall have been given by the acting party to the affected party and to the Securities and Exchange Commission, Washington, D.C., not less than sixty (60) days prior to the effective date of such termination.

If the Bond is for a joint ASSURED, it shall not be terminated unless written notice shall have been given by the acting party to the affected party, and by the COMPANY to all ASSURED **Investment Companies** and to the Securities and Exchange Commission, Washington, D.C., not less than sixty (60) days prior to the effective date of such termination.

This Bond will terminate as to any one ASSURED, other than an **Investment Company**:

- a. immediately on the taking over of such ASSURED by a receiver or other liquidator or by State or Federal officials, or
- b. immediately on the filing of a petition under any State or Federal statute relative to bankruptcy or reorganization of the ASSURED, or assignment for the benefit of creditors of the ASSURED, or
- c. immediately upon such ASSURED ceasing to exist, whether through merger into another entity, disposition of all of its assets or otherwise.

The COMPANY shall refund the unearned premium computed at short rates in accordance with the standard short rate cancellation tables if terminated by the ASSURED or pro rata if terminated for any other reason.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 17 of 19



*Conditions And*

*Limitations*

*Termination*

*(continued)*

If any partner, director, trustee, or officer or supervisory employee of an ASSURED not acting in collusion with an **Employee** learns of any dishonest act committed by such **Employee** at any time, whether in the employment of the ASSURED or otherwise, whether or not such act is of the type covered under this Bond, and whether against the ASSURED or any other person or entity, the ASSURED:

- a. shall immediately remove such **Employee** from a position that would enable such **Employee** to cause the ASSURED to suffer a loss covered by this Bond; and
- b. within forty-eight (48) hours of learning that an **Employee** has committed any dishonest act, shall notify the COMPANY, of such action and provide full particulars of such dishonest act.

The COMPANY may terminate coverage as respects any **Employee** sixty (60) days after written notice is received by each ASSURED **Investment Company** and the Securities and Exchange Commission, Washington, D.C. of its desire to terminate this Bond as to such **Employee**.

*Other Insurance*

14. Coverage under this Bond shall apply only as excess over any valid and collectible insurance, indemnity or suretyship obtained by or on behalf of:

- a. the ASSURED,
- b. a **Transportation Company**, or
- c. another entity on whose premises the loss occurred or which employed the person causing the loss or engaged the messenger conveying the **Property** involved.

*Conformity*

15. If any limitation within this Bond is prohibited by any law controlling this Bond's construction, such limitation shall be deemed to be amended so as to equal the minimum period of limitation provided by such law.

*Change or Modification*

16. This Bond or any instrument amending or affecting this Bond may not be changed or modified orally. No change in or modification of this Bond shall be effective except when made by written endorsement to this Bond signed by an authorized representative of the COMPANY.

If this Bond is for a sole ASSURED, no change or modification which would adversely affect the rights of the ASSURED shall be effective prior to sixty (60) days after written notice has been furnished to the Securities and Exchange Commission, Washington, D.C., by the acting party.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 18 of 19

***Conditions And***

***Limitations***

*Change or Modification (continued)*      If this Bond is for a joint ASSURED, no charge or modification which would adversely affect the rights of the ASSURED shall be effective prior to sixty (60) days after written notice has been furnished to all insured **Investment Companies** and to the Securities and Exchange Commission, Washington, D.C., by the COMPANY.

ICAP Bond (5-98)

Form 17-02-1421 (Ed. 5-98) Page 19 of 19

*Important Notice:*

**The SEC Requires Proof of Your Fidelity Insurance Policy**

Your company is now required to file an electronic copy of your fidelity insurance coverage (Chubb's ICAP Bond policy) to the Securities and Exchange Commission (SEC), according to rules adopted by the SEC on June 12, 2006.

Chubb is in the process of providing your agent/broker with an electronic copy of your insurance policy as well as instructions on how to submit this proof of fidelity insurance coverage to the SEC. You can expect to receive this information from your agent/broker shortly.

The electronic copy of your policy is provided by Chubb solely as a convenience and does not affect the terms and conditions of coverage as set forth in the paper policy you receive by mail. The terms and conditions of the policy mailed to you, which are the same as those set forth in the electronic copy, constitute the entire agreement between your company and Chubb.

If you have any questions, please contact your agent or broker.

Form 14-02-12160 (ed. 7/2006)

**POLICYHOLDER**  
**DISCLOSURE NOTICE OF**  
**TERRORISM INSURANCE COVERAGE**

**(for policies with no terrorism exclusion or sublimit)**

You are hereby notified that, under the Terrorism Risk Insurance Act (the Act), effective December 26, 2007, this policy makes available to you insurance for losses arising out of certain acts of terrorism. Terrorism is defined as any act certified by the Secretary of the Treasury, in concurrence with the Secretary of State and the Attorney General of the United States, to be an act of terrorism; to be a violent act or an act that is dangerous to human life, property or infrastructure; to have resulted in damage within the United States, or outside the United States in the case of an air carrier or vessel or the premises of a United States Mission; and to have been committed by an individual or individuals as part of an effort to coerce the civilian population of the United States or to influence the policy or affect the conduct of the United States Government by coercion.

You should know that the insurance provided by your policy for losses caused by acts of terrorism is partially reimbursed by the United States under the formula set forth in the Act. Under this formula, the United States pays 85% of covered terrorism losses that exceed the statutorily established deductible to be paid by the insurance company

providing the coverage.

However, if aggregate insured losses attributable to terrorist acts certified under the Act exceed \$100 billion in a Program Year (January 1 through December 31), the Treasury shall not make any payment for any portion of the amount of such losses that exceeds \$100 billion.

10-02-1281 (Ed. 1/2003)

## Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

---

If aggregate insured losses attributable to terrorist acts certified under the Act exceed \$100 billion in a Program Year (January 1 through December 31) and we have met our insurer deductible under the Act, we shall not be liable for the payment of any portion of the amount of such losses that exceeds \$100 billion, and in such case insured losses up to that amount are subject to pro rata allocation in accordance with procedures established by the Secretary of the Treasury.

The portion of your policy's annual premium that is attributable to insurance for such acts of terrorism is: \$ **-0-**.

If you have any questions about this notice, please contact your agent or broker.

10-02-1281 (Ed. 1/2003)

**ENDORSEMENT/RIDER**

Effective date of

this endorsement/rider: December 22, 2011

**FEDERAL INSURANCE COMPANY**

Endorsement/Rider No. 1

To be attached to and  
form a part of Bond No. 82302678

Issued to: STONE HARBOR EMERGING MARKETS INCOME FUND

**COMPLIANCE WITH APPLICABLE TRADE SANCTION LAWS**

It is agreed that this insurance does not apply to the extent that trade or economic sanctions or other similar laws or regulations prohibit the coverage provided by this insurance.

The title and any headings in this endorsement/rider are solely for convenience and form no part of the

terms and conditions of coverage.

All other terms, conditions and limitations of this Bond shall remain unchanged.

14-02-9228 (02/2010)

Page 1

**ENDORSEMENT/RIDER**

Effective date of

this endorsement/rider: December 22, 2011

**FEDERAL INSURANCE COMPANY**

Endorsement/Rider No. 2

To be attached to and  
form a part of Bond No. 82302678

Issued to: STONE HARBOR EMERGING MARKETS INCOME FUND

**DELETING VALUATION-OTHER PROPERTY AND AMENDING CHANGE OR MODIFICATION ENDORSEMENT**

In consideration of the premium charged, it is agreed that this Bond is amended as follows:

1. The paragraph titled Other Property in Section 9, Valuation, is deleted in its entirety.
2. The third paragraph in Section 16, Change or Modification, is deleted in its entirety and replaced with the following: If this Bond is for a joint ASSURED, no change or modification which would adversely affect the rights of the ASSURED shall be effective prior to sixty (60) days after written notice has been furnished to all insured **Investment Companies** and the Securities and Exchange Commission, Washington, D.C., by the COMPANY.

The title and any headings in this endorsement/rider are solely for convenience and form no part of the terms and conditions of coverage.

All other terms, conditions and limitations of this Bond shall remain unchanged.

17-02-2437 (12/2006) rev.

Page 1

**FEDERAL INSURANCE COMPANY**

Endorsement No:

3

Bond Number:

82302678

NAME OF ASSURED: STONE HARBOR EMERGING MARKETS INCOME FUND  
**TERMINATION-NONRENEWAL-NOTICE ENDORSEMENT**

It is agreed that this Bond is amended as follows:

1. By adding to Section 13., Termination, the following:  
Termination By The Company

**Bonds In Effect For More Than Sixty (60) Days**

If this Bond has been in effect for more than sixty (60) days, or, if this Bond is a renewal, the COMPANY may terminate by providing written notice of cancellation at least sixty (60) days before the effective date of termination for at least one of the following reasons:

1. Nonpayment of premium;
2. Discovery of fraud or material misrepresentation in obtaining this Bond or in the presentation of a claim thereunder;
3. Discovery of willful or reckless acts or omissions or violation of any provision of this Bond on the part of the ASSURED which substantially and materially increases any hazard insured against, and which occurred subsequent to the inception of the current BOND PERIOD;
4. Conviction of the ASSURED of a crime arising out of acts increasing the hazard insured against;
5. Material change in the risk which increases the risk of loss after insurance coverage has been issued or renewed, except to the extent that the COMPANY should reasonably have foreseen the change, or contemplated the risk when the contract was written;
6. Determination by the Commissioner that the continuation of the Bond would jeopardize a COMPANY S solvency or would place the COMPANY in violation of the insurance laws of any state;
7. Determination by the Commissioner that continuation of the present premium volume of the COMPANY would jeopardize the COMPANY S policyholders, creditors or the public;
8. Such other reasons that are approved by the Commissioner;
9. Determination by the Commissioner that the COMPANY no longer has adequate reinsurance to meet the ASSURED S needs;
10. Substantial breaches of contractual duties, conditions or warranties; or
11. Unfavorable underwriting facts, specific to the ASSURED, existing that were not present at the inception of the Bond.

ICAP Bond



Bonds In Effect Sixty (60) Days Or Less

If this Bond has been in effect for sixty (60) days or less, and it is not a renewal Bond, the COMPANY may terminate for any reason by providing written notice of termination at least sixty (60) days before the effective date of termination. Notice Of Termination

Notice of termination under this Section shall be mailed or delivered, by certified mail, return receipt provided by the United States Postal Service, to the ASSURED and to the authorized agent or broker, if any, at least sixty (60) days prior to the effective date of cancellation at the address shown on the DECLARATIONS of this Bond.

If this Bond is cancelled for nonpayment of premium, the COMPANY will mail or deliver, by certified mail, return receipt provided by the United States Postal Service, a written notice at least thirty (30) days before the effective date of cancellation. The cancellation notice shall contain information regarding the amount of premium due and the due date, and shall state the effect of nonpayment by the due date. Cancellation shall not be effective if payment of the amount due is made prior to the effective date of cancellation.

All notice of cancellation shall state the reason(s) for cancellation.

There is no liability on the part of, and no cause of action of any nature shall arise against, the COMPANY, its authorized representatives, its employees, or any firm, person or corporation furnishing to the COMPANY, information relating to the reasons for cancellation or nonrenewal, for any statement made by them in complying or enabling the COMPANY to comply with this Section, for the provision of information pertaining thereto, or for statements made or evidence submitted at any hearings conducted in connection therewith, if such information was provided in good faith and without malice.

Notice Of Nonrenewal

If the COMPANY elects not to renew this Bond, the COMPANY shall mail or deliver written notice, by certified mail, return receipt, provided by the United States Postal Service, to the ASSURED, at his last known address, at least sixty (60) days before the expiration date or before the anniversary date, if this Bond has been written for a term of more than one (1) year. Such notice shall also be mailed to the ASSURED S agent or broker, if any.

Such notice shall contain all of the following:

- a. Bond Number;
- b. Date of Notice;
- c. Reason for Cancellation;
- d. Expiration Date of the Bond;
- e. Effective Date and Hour of Cancellation.

Notice of nonrenewal shall not be required if the COMPANY or a COMPANY within the same insurance group has offered to issue a renewal Bond, the ASSURED has obtained replacement coverage or has agreed in writing to obtain replacement coverage, the ASSURED has requested or agreed to nonrenewal, or the Bond is expressly designated as nonrenewable.

ICAP Bond

Return Premium Calculations

Any unearned premiums which have been paid by the ASSURED shall be refunded to the ASSURED on a pro rata basis if terminated by the COMPANY or the ASSURED. The unearned premiums shall be refunded to the ASSURED within forty-five (45) days of receipt of the request for cancellation or the effective date of cancellation, whichever is later.

Conditional Renewal

If the COMPANY offers or purports to renew the Bond, but on less favorable terms or at higher rates, the new terms or higher premiums may take effect on the renewal date, if the COMPANY mails or delivers by certified mail, return receipt provided by the United States Postal Service, to the ASSURED, notice of the new terms or premiums at least sixty (60) days prior to the renewal date. If the COMPANY notifies the ASSURED within sixty (60) days prior to the renewal date, the new terms or premiums do not take effect until sixty (60) days after the notice is mailed or delivered, in which case, the ASSURED may elect to cancel the renewal Bond within the sixty (60) day period. If the COMPANY does not notify the ASSURED of the new terms or premiums, the COMPANY shall continue the Bond at the expiring terms and premiums until notice is given or until the effective date of replacement coverage is obtained by the ASSURED, whichever occurs first.

2. It is further understood and agreed that for the purposes of Section 13., Termination, any occurrence listed in this Section shall be considered to be a request by the ASSURED to immediately terminate this Bond.

This Endorsement applies to loss discovered after 12:01 a.m. on December 22, 2011.

ALL OTHER TERMS AND CONDITIONS OF THIS BOND REMAIN UNCHANGED.

Date: February 1, 2012

ICAP Bond

Form 17-02-1360 (Rev. 10-99) Page 3

**Stone Harbor Emerging Markets Income Fund**

( **Stone Harbor EMI Fund** )

**Fidelity Bond Resolutions**

**October 19, 2011**

**RESOLVED**, that, after considering all relevant factors, the action of the Stone Harbor EMI Fund in purchasing an Investment Company Blanket Bond issued by Federal Insurance Company (Chubb), covering larceny and embezzlement and certain other acts, in the amounts and on the terms presented to the Trustees, be, and it hereby is, approved;

**FURTHER RESOLVED**, that pursuant to Rule 17g-1 under the 1940 Act, the President, any Vice President, the Treasurer, the Secretary and any Assistant Secretary be, and each of them acting singly hereby is, designated as an agent for the Stone Harbor EMI Fund to make the filings and to give the notices required by subparagraph (g) of such Rule 17g-1;

**FURTHER RESOLVED**, that the form and amount of the Investment Company Blanket Bond, after consideration of all relevant factors, including the Stone Harbor EMI Fund's aggregate assets to which persons covered by the bond have access, the type and terms of arrangements made for custody and safekeeping of assets, and the nature of the securities held, be, and they hereby are, approved; and

**FINALLY RESOLVED**, that the officers of the Stone Harbor EMI Fund be, and each of them acting singly hereby is, authorized in the name and on behalf of this Stone Harbor EMI Fund to do and to perform all such acts and things, to execute, to seal and to deliver and, where necessary or appropriate, to file with the appropriate governmental authorities all such further certificates, contracts, agreements, documents, instruments, powers of attorney, receipts or other papers and to take such other action and to make all such payments, as the officer or officers so acting shall determine in their judgment, or in the judgment of any of them, to be necessary or appropriate to carry out, to comply with or to effectuate the purposes and intents of the transactions and other matters contemplated by the foregoing resolutions, the taking of such action by such officer or officers to be conclusive evidence of its authorization hereby; and that all actions of the officers of the Stone Harbor EMI Fund taken in connection with the establishment, organization or operation of the Stone Harbor EMI Fund, be, and they hereby are, ratified, approved and confirmed in all respects.

Opt;">

Basic

\$

0.10

\$

0.15

\$

0.17

\$

0.31

Diluted

\$

0.10

\$

0.15

\$

0.17

\$

0.30

Weighted average shares outstanding:

Basic

51,887,094

51,633,150

51,884,402

51,578,691

Diluted

52,019,881

52,223,183

51,996,263

52,111,134

Dividends declared per share

\$

0.05

\$

0.05

\$

0.05

\$

0.05

See accompanying Notes to Consolidated Financial Statements.





Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income

(dollars in thousands)

(unaudited)

	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
Net income	\$ 4,958	\$ 7,723	\$ 8,969	\$ 15,732
Currency translation adjustment	(37)	3	(7)	8
Other comprehensive income	(37)	3	(7)	8
Comprehensive income	\$ 4,921	\$ 7,726	\$ 8,962	\$ 15,740

See accompanying Notes to Consolidated Financial Statements.

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Consolidated Statements of Stockholders' Equity (Deficit)

(dollars in thousands, except share data)

(unaudited)

	Common stock					Accumulated other comprehensive income	
	Shares	Amount	Additional paid-in capital	Treasury units	Retained earnings (deficit)	(loss)	Total
Balance at December 31, 2016	51,607,143	\$ 5	\$ 185,998	\$ -	\$ (47,058)	\$ (46)	\$ 138,899
Issuance of restricted shares	324,184	-	-	-	-	-	-
Cancellation of restricted shares	(87,849)	-	-	-	-	-	-
Stock based compensation	-	-	3,156	-	-	-	3,156
Stock option exercises	313,372	-	1,639	-	-	-	1,639
Tax withholdings related to net share settlements of stock based compensation awards	-	-	(318)	-	-	-	(318)
Dividends paid	-	-	(10,366)	-	-	-	(10,366)
Foreign currency translation adjustments	-	-	-	-	-	45	45
Net income	-	-	-	-	10,819	-	10,819
Balance at December 31, 2017	52,156,850	\$ 5	\$ 180,109	\$ -	\$ (36,239)	\$ (1)	\$ 143,874
Adoption of revenue recognition standard (see Note 1)	-	-	-	-	(60)	-	(60)
Issuance of restricted shares	395,282	-	-	-	-	-	-
Cancellation of restricted shares	(44,042)	-	-	-	-	-	-
Stock based compensation	-	-	1,215	-	-	-	1,215
Dividends paid	-	-	(5,200)	-	-	-	(5,200)
Foreign currency translation adjustments	-	-	-	-	-	(7)	(7)
Net income	-	-	-	-	8,969	-	8,969
Balance at June 30, 2018	52,508,090	\$ 5	\$ 176,124	\$ -	\$ (27,331)	\$ (8)	\$ 148,790

See accompanying Notes to Consolidated Financial Statements.



Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(dollars in thousands)

(unaudited)

	Six Months Ended June 30,	
	2018	2017
Cash Flows From Operating Activities		
Net income	\$ 8,969	\$ 15,732
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation & amortization	13,978	12,592
Amortization of debt issuance costs	338	349
Loss on disposals of property, plant and equipment	344	152
Deferred rent	1,877	1,552
Stock based compensation	1,215	1,770
Deferred income taxes	1,019	2,523
Changes in operating assets and liabilities:		
Receivables	(836)	(610)
Inventories	(15,167)	7,009
Prepaid expenses and other assets	(1,217)	5,139
Accounts payable	2,016	(1,015)
Income tax receivable / payable	2,281	382
Accrued expenses and other liabilities	4,459	(10,747)
Net cash provided by operating activities	19,276	34,828
Cash Flows From Investing Activities		
Purchases of property, plant and equipment	(13,149)	(20,000)
Proceeds from the sale of property, plant and equipment	15	-
Net cash used in investing activities	(13,134)	(20,000)
Cash Flows From Financing Activities		
Payments of long-term debt and capital lease obligations	(32,638)	(34,646)
Advances on line of credit	35,000	25,000
Dividends paid	(5,200)	(5,168)
Proceeds from exercise of stock options	-	102
Employee taxes paid for shares withheld	(30)	(211)
Net cash used in financing activities	(2,868)	(14,923)
Effect of exchange rate changes on cash	(8)	8
Net change in cash	3,266	(87)

Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

Cash, cash equivalents and restricted cash beginning of period	7,476	12,948
Cash, cash equivalents and restricted cash end of period	\$ 10,742	\$ 12,861
Cash and cash equivalents	\$ 9,907	\$ 12,006
Restricted cash	835	855
Long-term restricted cash	-	-
Cash, cash equivalents and restricted cash end of period	\$ 10,742	\$ 12,861
Supplemental disclosure of cash flow information		
Purchases of property, plant and equipment included in accounts payable and accrued expenses	\$ 1,488	\$ 2,407
Cash paid for interest	1,124	936
Cash paid (received) for income taxes, net	186	5,817

See accompanying Notes to Consolidated Financial Statements.

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

Note 1: Background

Tile Shop Holdings, Inc. (“Holdings,” and together with its wholly owned subsidiaries, the “Company”) was incorporated in Delaware in June 2012.

The Company is a specialty retailer of natural stone and man-made tiles, setting and maintenance materials, and related accessories in the United States. The Company manufactures its own setting and maintenance materials, such as thinset, grout, and sealers. The Company’s primary market is retail sales to consumers, contractors, designers and home builders. As of June 30, 2018, the Company had 140 stores in 31 states and the District of Columbia, with an average size of approximately 20,200 square feet. The Company also sells products on its website. The Company has distribution centers located in Michigan, New Jersey, Oklahoma, Virginia and Wisconsin. The Company has a sourcing operation located in China.

The accompanying Consolidated Financial Statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the rules and regulations for reporting on Form 10-Q. Accordingly, they do not include certain information and disclosures required for comprehensive financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal recurring nature, including the elimination of all intercompany transactions. Operating results for the three and six months ended June 30, 2018 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2018.

These statements should be read in conjunction with the Consolidated Financial Statements and footnotes included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. The accounting policies used in preparing these Consolidated Financial Statements are the same as those described in Note 1 to the Consolidated Financial Statements in such Form 10-K.

Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued a final standard on revenue from contracts with customers. This new standard introduces a comprehensive revenue recognition model that requires a company to recognize revenue to depict the transfer of goods or services to a customer at an amount that reflects the consideration it expects to receive in exchange for those goods or services. In 2016, the FASB issued several amendments to the standard. The Company adopted this standard as of January 1, 2018 using the modified retrospective transition method. See Note 2 for further details.

In November 2016, the FASB issued new guidance on restricted cash on the statement of cash flows. The new guidance requires the classification and presentation of changes in restricted cash and cash equivalents in the statement of cash flows. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning and ending balances shown in the statement of cash flows. The Company adopted the new standard as of March 31, 2018 using the retrospective transition method. The Company’s restricted cash balance was \$0.8 million as of June 30, 2018. Upon adopting the new standard, the Company no longer presents the release of restricted cash as a financing cash inflow. Instead, restricted cash and long-term restricted cash balances are included in the beginning and ending cash, cash equivalents and restricted cash balances in the Consolidated Statement of Cash Flows. In connection with the adoption of this standard, \$6.0 million received from restricted cash accounts during the six months ended June 30, 2017 that was previously presented as a financing cash inflow was reclassified to the beginning cash, cash equivalents and restricted cash balances in the Consolidated Statement of Cash Flows.

#### Accounting Pronouncements Not Yet Adopted

In February 2016, the FASB issued a standard that primarily requires organizations that lease assets to recognize the rights and obligations created by those leases on the consolidated balance sheet. The standard is effective in fiscal year 2019, with early adoption permitted. The Company expects the primary impact upon adoption will be the recognition, on a discounted basis, of minimum commitments under non-cancelable operating leases on the consolidated balance sheets resulting in the recording of right of use assets and lease obligations. The Company’s minimum commitments under non-cancelable operating leases are disclosed in Note 5 to the Consolidated Financial Statements included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2017. The Company has identified its lease management system and is in the process of identifying and evaluating the applicable leases. The Company is currently assessing the effect the new standard will have on its consolidated financial statements.

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

Note 2: Revenues

On January 1, 2018, the Company adopted Accounting Standards Update No. 2014-09 (Topic 606), “Revenue from Contracts with Customers,” using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with the Company’s historic accounting under Topic 605. The adoption of Topic 606 had a cumulative impact adjustment to opening retained earnings of \$0.1 million as of January 1, 2018 and did not have an impact on revenues recognized for the three and six months ended June 30, 2018.

Revenue Recognition

Revenues are recognized when control of the promised goods or services is transferred to our customers, in an amount that reflects the consideration received in exchange for those goods or services. Sales taxes are excluded from revenues.

The following table presents revenues disaggregated by product category:

	For the three months ended June 30,		For the six months ended June 30,	
	2018	2017	2018	2017
Man-made tiles	47 %	43 %	46 %	42 %
Natural stone tiles	28	33	28	34
Setting and maintenance materials	13	11	13	11
Accessories	10	11	11	11
Delivery service	2	2	2	2



Total 100 % 100 % 100 % 100 %

The Company generates revenues by selling tile products, setting and maintenance materials, accessories, and delivery services to its customers through its store locations and website. The timing of revenue recognition coincides with the transfer of control of goods and services ordered by the customer, which falls into one of three categories described below:

- Revenue recognized when an order is placed – If a customer places an order in a store and the contents of their order are available, the Company recognizes revenue concurrent with the exchange of goods for consideration from the customer.
- Revenue recognized when an order is picked up – If a customer places an order for items held in a centralized distribution center, the Company requests a deposit from the customer at the time they place the order. Subsequently when the contents of the customer’s order are delivered to the store, the customer returns to the store and picks up the items that were ordered. The Company recognizes revenue on this transaction when the customer picks up their order.
- Revenue recognized when an order is delivered – If a customer places an order in a store or online and requests delivery of their order, the Company prepares the contents of their order, initiates the delivery service, and recognizes revenue once the contents of the customer’s order are delivered.

The Company determines the transaction price of its contracts based on the pricing established at the time a customer places an order. The transaction price does not include sales tax as the Company is a pass-through conduit for collecting and remitting sales tax. Any discounts applied to an order are allocated proportionately to the base price of the goods and services ordered. Deposits made by customers are recorded in other accrued liabilities. Deferred revenues associated with customer deposits are recognized at the time the Company transfers control of the items ordered or renders the delivery service. In the event an order is partially fulfilled as of the end of a reporting period, revenue will be recognized based on the transaction price allocated to the goods delivered and services rendered. The customer deposit balance was \$8.1 million as of each of June 30, 2018 and December 31, 2017. Revenues recognized during the six months ended June 30, 2018 included in the customer deposit balance as of the beginning of the period were \$7.7 million.

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

The Company extends financing to qualified professional customers who apply for credit. The accounts receivable balance was \$3.2 million and \$2.4 million as of June 30, 2018 and December 31, 2017, respectively. Customers who qualify for an account receive 30-day payment terms. The Company expects that the customer will pay for the goods and services ordered within one year from the date the order is placed. Accordingly, the Company qualifies for the practical expedient outlined in ASC 606-10-32-18 and does not adjust the promised amount of consideration for the effects of the financing component.

Customers may return purchased items for an exchange or refund. The Company records a reserve for estimated product returns based on the historical returns trends and the current product sales performance. Historically, the sales returns reserve was presented net of cost of sales in other current liabilities. Upon adoption of Topic 606, the Company presents the sales returns reserve as an other current liability and the estimated value of the inventory that will be returned as an other current asset in the Consolidated Balance Sheet. The components of the sales returns reserve reflected in the Consolidated Balance Sheet as of June 30, 2018 and December 31, 2017 are as follows:

	(in thousands)	
	June 30, 2018	December 31, 2017(1)
Other current liabilities	\$ 5,792	\$ 3,139
Other current assets	1,651	-
Sales returns reserve, net	\$ 4,141	\$ 3,139

(1) As of December 31, 2017, the sales returns reserve of \$3.1 million was presented net of the expected value of inventory to be returned of \$0.9 million.

## Note 3: Inventories

Inventories are stated at the lower of cost (determined on the weighted-average cost method) or net realizable value. Inventories consist primarily of merchandise held for sale. Inventories were comprised of the following as of June 30,

2018 and December 31, 2017:

	(in thousands)	
	June 30, 2018	December 31, 2017
Finished goods	\$ 83,521	\$ 65,843
Raw materials	2,288	1,660
Finished goods in transit	14,617	17,756
Total	\$ 100,426	\$ 85,259

The Company provides provisions for losses related to shrinkage and other amounts that are otherwise not expected to be fully recoverable. These provisions are calculated based on historical shrinkage, selling price, margin and current business trends. The provision for losses related to shrinkage and other amounts was \$0.5 million and \$0.2 million as of June 30, 2018 and December 31, 2017, respectively.

#### Note 4: Income taxes

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the "Tax Act") was enacted into law and the new legislation contains several key tax provisions that affected the Company, including, but not limited to, a reduction of the corporate income tax rate to 21% effective January 1, 2018, and a one-time mandatory transition tax on accumulated foreign earnings, a tax on global intangible low taxed income ("GILTI"), and the repeal of the domestic manufacturing deduction for 2018. The Company recognized the effect of the tax law changes in the period of enactment, including determining the transition tax, re-measuring the Company's U.S. deferred tax assets and liabilities and reassessing the net realizability of the Company's deferred tax assets and liabilities. Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act, ("SAB 118") allows the Company to record provisional amounts during a measurement period not to extend beyond one year of the enactment date. Since the Tax Act was passed late in the fourth quarter of 2017, and ongoing guidance and accounting interpretation is expected throughout 2018, the Company considers the accounting of the transition tax, deferred tax re-measurements and other items to be provisional due to the forthcoming guidance and the Company's ongoing analysis of final year-end data and tax positions. The Company expects to complete its analysis

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

within the measurement period in accordance with SAB 118. While the Company does not expect to incur a current tax on GILTI relative to 2018 operations, the Company has not yet elected an accounting policy related to GILTI.

The Company's effective tax rate on net income before income taxes for the three months ended June 30, 2018 and 2017 was 28.0% and 31.1%, respectively. The Company's effective tax rate on net income before taxes for the six months ended June 30, 2018 and 2017 was 28.1% and 35.3%, respectively. The difference between the Company's effective rate of 28.0% and the expected federal statutory rate of 21.0% for the three and six months ended June 30, 2018 is primarily due to state income taxes.

For the three months ended June 30, 2018 and 2017, the Company recorded a provision for income taxes of \$1.9 million and \$3.5 million, respectively. For the six months ended June 30, 2018 and 2017, the Company recorded a provision for income taxes of \$3.5 million and \$8.6 million, respectively. The decrease in the provision for income taxes for both the three and six months ended June 30, 2018 and 2017 is due to lower pretax earnings as well as the decrease in the corporate tax rate.

The Company records interest and penalties relating to uncertain tax positions in income tax expense. As of June 30, 2018 and 2017, the Company has not recognized any liabilities for uncertain tax positions, nor have interest and penalties related to uncertain tax positions been accrued.

Note 5: Earnings Per Share

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

Basic and diluted earnings per share were calculated as follows:

	(all amounts in thousands except share and per share data)			
	For the three months ended		For the six months ended	
	June 30, 2018	2017	June 30, 2018	2017
Net income	\$ 4,958	\$ 7,723	\$ 8,969	\$ 15,732
Weighted average shares outstanding - basic	51,887,094	51,633,150	51,884,402	51,578,691
Effect of dilutive securities attributable to stock based awards	132,787	590,033	111,861	532,443
Weighted average shares outstanding - diluted	52,019,881	52,223,183	51,996,263	52,111,134
Income per common share:				
Basic	\$ 0.10	\$ 0.15	\$ 0.17	\$ 0.31
Dilutive	\$ 0.10	\$ 0.15	\$ 0.17	\$ 0.30
Anti-dilutive securities excluded from earnings per share calculation	2,298,350	209,570	2,107,629	254,511

Note 6: Other Accrued Liabilities

Other accrued liabilities consisted of the following:

	(in thousands)	
	June 30, 2018	December 31, 2017
Customer deposits	\$ 8,080	\$ 8,064
Accrued wages and salaries	3,795	2,853
Sales returns reserve	5,792	3,139
Payroll and sales taxes	3,233	2,491
Other current liabilities	6,237	5,866
Total other accrued liabilities	\$ 27,137	\$ 22,413

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

Note 7: Long-term Debt

On June 2, 2015, Holdings and its operating subsidiary, The Tile Shop, LLC, entered into a credit agreement with Fifth Third Bank, Bank of America, N.A., and Huntington National Bank (as amended, the “Credit Agreement”). The Credit Agreement was most recently amended on April 5, 2018 to adjust the consolidated fixed charge coverage ratio covenant to a minimum of 1.35:1.00 and revise the consolidated total rent adjusted leverage ratio covenant to a maximum of 4.00:1.00.

The Credit Agreement provides the Company with a \$125.0 million senior secured credit facility, comprised of a five-year \$50.0 million term loan and a \$75.0 million revolving line of credit. Borrowings outstanding consisted of \$7.0 million on the term loan and \$22.5 million on the revolving line of credit as of June 30, 2018. There was \$52.5 million available for borrowing on the revolving line of credit as of June 30, 2018, which may be used to support the Company’s growth and for working capital purposes.

Borrowings pursuant to the Credit Agreement bear interest at either a base rate or a LIBOR-based rate, at the option of the Company. The LIBOR-based rate will range from LIBOR plus 1.50% to 2.00%, depending on The Tile Shop’s leverage ratio. The base rate is equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Fifth Third Bank “prime rate,” and (c) the Eurodollar rate plus 1.00%, in each case plus 0.50% to 1.00% depending on The Tile Shop’s leverage ratio. At June 30, 2018 the base interest rate was 5.75% and the LIBOR-based interest rate was 3.84%.

The term loan requires quarterly principal payments of \$2.5 million for quarters ended September 30, 2018 through March 31, 2020. The Company can elect to prepay the term loan without incurring a penalty.

The Credit Agreement is secured by virtually all of the assets of the Company, including but not limited to, inventory, receivables, equipment and real property. The Credit Agreement contains customary events of default, conditions to borrowings, and restrictive covenants, including restrictions on the Company’s ability to dispose of assets, make acquisitions, incur additional debt, incur liens, make investments, or enter into transactions with affiliates on other than terms that could be obtained in an arm’s length transaction. The Credit Agreement also includes financial and other covenants including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios.

Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

The Company was in compliance with the covenants as of June 30, 2018.

The Company has standby letters of credit outstanding related to its workers compensation and medical insurance policies. As of June 30, 2018 and 2017, the standby letters of credit totaled \$1.1 million.

Long-term debt consisted of the following at June 30, 2018 and December 31, 2017 (in thousands):

	June 30, 2018		December 31, 2017	
	Principal	Unamortized Debt Issuance Costs	Principal	Unamortized Debt Issuance Costs
Term note payable - interest at 3.84% and 3.06% at June 30, 2018 and December 31, 2017, respectively	\$ 6,971	\$ (15)	\$ 11,346	\$ (36)
Commercial bank credit facility	22,500	-	15,000	-
Variable interest rate bonds (1.69% at December 31, 2017)	-	-	705	-
Total debt obligations	29,471	(15)	27,051	(36)
Less: current portion	6,971	(13)	8,855	(22)
Debt obligations, net of current portion	\$ 22,500	\$ (2)	\$ 18,196	\$ (14)

Note 8: Fair Value of Financial Instruments

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

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





Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

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

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

Level 3 – Significant unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment.

The following table sets forth by Level within the fair value hierarchy the Company’s financial assets that were accounted for at fair value on a recurring basis at June 30, 2018 and December 31, 2017 according to the valuation techniques the Company uses to determine their fair values. There have been no transfers of assets among the fair value hierarchies presented.

	Pricing	Fair Value at	
	Category	June 30, 2018	December 31, 2017
	(in thousands)		
Assets			
Cash and cash equivalents	Level 1	\$ 9,907	\$ 6,621
Restricted cash	Level 1	835	855

The following methods and assumptions were used to estimate the fair value of each class of financial instrument. There have been no changes in the valuation techniques used by the Company to value the Company’s financial instruments.

- Cash and cash equivalents: Consists of cash on hand and bank deposits. The value was measured using quoted market prices in active markets. The carrying amount approximates fair value.

- Restricted cash: Consists of cash and cash equivalents held in bank deposit accounts restricted as to withdrawal or that are under the terms of use for current operations. The value was measured using quoted market prices in active markets. The carrying amount approximates fair value.

Fair value measurements also apply to certain non-financial assets and liabilities measured at fair value on a nonrecurring basis. Property, plant and equipment is measured at fair value when an impairment is recognized and the related assets are written down to fair value. The Company measured the fair value of these assets based on projected cash flows and an estimated risk-adjusted rate of return. Projected cash flows are considered level 3 inputs. During the three and six months ended June 30, 2018, the Company identified property, plant and equipment that would be disposed of prior to the end of their useful lives, which resulted in the recognition of a \$0.3 million charge to write-down these assets to their estimated fair value. No impairment charges were recorded during the three and six months ended June 30, 2017.

The carrying value of the Company's borrowings under its credit agreement approximate fair value based upon Level 2 inputs of the market interest rates available to the Company for debt obligations with similar risks and maturities.

#### Note 9: Equity Incentive Plans

##### Stock options:

The Company measures and recognizes compensation expense for all stock based awards at fair value. The financial statements for the three and six months ended June 30, 2018 and 2017 include compensation cost for the portion of outstanding awards that vested during those periods. The Company recognizes stock based compensation costs on a straight-line basis over the requisite service period of the award, which is generally the option vesting term. Total stock based compensation expense related to stock options was \$0.2 million and \$0.6 million for the three months ended June 30, 2018 and 2017, respectively. Total stock based compensation expense related to stock options was \$0.5 million and \$1.2 million for the six months ended June 30, 2018 and 2017, respectively. Stock based compensation expense pertaining to stock options is included in selling, general and administrative expenses in the accompanying Consolidated Statements of Income.

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

As of June 30, 2018, the Company had outstanding stock options to purchase 1,672,804 shares of common stock at a weighted average exercise price of \$14.44.

Restricted stock:

The Company awards restricted common shares to selected employees and to non-employee directors. Recipients are not required to provide any consideration other than continued service. Restricted stock awards are subject to certain restrictions on transfer, and all or part of the shares awarded may be subject to forfeiture upon the occurrence of certain events, including employment termination. Certain awards are also subject to forfeiture if the Company fails to attain certain performance targets. The restricted stock is valued at its grant date fair value and expensed over the requisite service period or the vesting term of the awards. The Company adjusts the cumulative expense recognized on awards with performance conditions based on the probability of achieving the performance condition. Total stock based compensation expense related to restricted stock was \$0.4 million and \$0.3 million for the three months ended June 30, 2018 and 2017, respectively. Total stock based compensation expense related to restricted stock was \$0.7 million and \$0.6 million for the six months ended June 30, 2018 and 2017, respectively. Stock based compensation expense pertaining to restricted stock is included in selling, general and administrative expenses in the accompanying Consolidated Statements of Income.

As of June 30, 2018, the Company had 618,091 outstanding restricted common shares.

Note 10: New Market Tax Credit

2016 New Market Tax Credit

In December 2016, the Company entered into a financing transaction with U.S. Bank Community, LLC (“U.S. Bank”) related to a \$9.2 million expansion of the Company’s facility in Durant, Oklahoma. U.S. Bank made a capital contribution to, and Tile Shop Lending, Inc. (“Tile Shop Lending”) made a loan to, Twain Investment Fund 192 LLC

(the “Investment Fund”) under a qualified New Markets Tax Credit (“NMTC”) program. The NMTC program was provided for in the Community Renewal Tax Relief Act of 2000 (the “Act”) and is intended to induce capital investment in qualified lower income communities. The Act permits taxpayers to claim credits against their Federal income taxes for up to 39% of qualified investments in the equity of community development entities (“CDEs”). CDEs are privately managed investment institutions that are certified to make qualified low-income community investments.

In this transaction, Tile Shop Lending loaned \$6.7 million to the Investment Fund at an interest rate of 1.37% per year and with a maturity date of December 31, 2046. The Investment Fund then contributed the loan to a CDE, which, in turn, loaned the funds on similar terms to Tile Shop of Oklahoma, LLC, an indirect, wholly-owned subsidiary of Holdings. The proceeds of the loans from the CDEs (including loans representing the capital contribution made by U.S. Bank, net of syndication fees) were used to partially fund the distribution center project.

In December 2016, U.S. Bank also contributed \$3.1 million to the Investment Funds and, by virtue of such contribution, is entitled to substantially all of the tax benefits derived from the NMTCs, while the Company effectively received net loan proceeds equal to U.S. Bank’s contributions to the Investment Fund. This transaction includes a put/call provision whereby the Company may be obligated or entitled to repurchase U.S. Bank’s interest. The Company believes that U.S. Bank will exercise the put option in December 2023 at the end of the recapture period. The value attributed to the put/call is de minimis. The NMTC is subject to 100% recapture for a period of seven years as provided in the Internal Revenue Code. The Company is required to be in compliance with various regulations and contractual provisions that apply to the NMTC arrangement. Non-compliance with applicable requirements could result in projected tax benefits not being realized and, therefore, could require the Company to indemnify U.S. Bank for any loss or recapture of NMTCs related to the financing until such time as the obligation to deliver tax benefits is relieved. The Company does not anticipate any credit recaptures will be required in connection with this arrangement.

The Company has determined that the financing arrangement with the Investment Fund and CDEs contains a variable interest entity (“VIE”). The ongoing activities of the Investment Fund – collecting and remitting interest and fees and NMTC compliance – were all considered in the initial design and are not expected to significantly affect economic performance throughout the life of the Investment Fund. Management considered the contractual arrangements that obligate the Company to deliver tax benefits and provide various other guarantees to the structure; U.S. Bank’s lack of a material interest in the underlying economics of the project; and the fact that the Company is obligated to absorb losses of the Investment Fund. The Company concluded that it is the primary beneficiary of the VIE and consolidated the Investment Fund, as a VIE, in accordance with the accounting standards for consolidation. In 2016, U.S. Bank’s contributions of \$3.1 million, net of syndications fees, were included in cash, restricted cash, other accrued liabilities and other long-term liabilities in the Consolidated Balance Sheet. The Company incurred \$1.2 million of

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

syndication fees in connection with this transaction, which were classified as other current assets and other non-current assets in the Consolidated Balance Sheet. The Company is recognizing the benefit of this net \$1.9 million contribution over the seven-year compliance period as it is being earned through the on-going compliance with the conditions of the NMTC program. As of June 30, 2018, the balance of the contribution liability was \$2.5 million, of which \$0.4 million is classified as other accrued liabilities on the Consolidated Balance Sheet and \$2.1 million is classified as other long-term liabilities on the Consolidated Balance Sheet.

The Company is able to request reimbursement for certain expenditures made in connection with the expansion of the distribution center in Durant, Oklahoma from the Investment Fund. Expenditures that qualify for reimbursement include building costs, equipment purchases, and other expenditures tied to the expansion of the facility. During the fiscal year ended December 31, 2017, the Company received reimbursements totaling \$6.0 million from the Investment Fund. As of June 30, 2018, the balance in the Investment Fund available for reimbursement to the Company was \$0.8 million.

#### 2013 New Market Tax Credit

In July 2013, the Company entered into a financing transaction with U.S. Bank and Chase Community Equity (“Chase”, and collectively with US. Bank, the “investors”) related to a \$19.1 million acquisition, rehabilitation, and construction of the Company’s distribution center and manufacturing facilities in Durant, Oklahoma. In this transaction, Tile Shop Lending loaned \$13.5 million to the Tile Shop Investment Fund LLC. The investors contributed \$5.6 million to the Tile Shop Investment Fund LLC. The investors are entitled to the tax benefits derived from the NMTC by virtue of their contribution while the Company received the proceeds, net of syndication fees, to apply toward the construction project. This transaction includes a put/call provision whereby the Company may be obligated or entitled to repurchase the investors’ interest. The Company believes that the investors will exercise the put option in September 2020 at the end of the recapture period. The value attributed to the put/call is de minimis. The NMTC is subject to 100% recapture for a period of seven years as provided in the Internal Revenue Code. The Company is required to be in compliance with various regulations and contractual provisions that apply to the NMTC arrangement. Non-compliance with applicable requirements could result in projected tax benefits not being realized and, therefore, could require the Company to indemnify the investors for any loss or recapture of NMTCs related to the financing until such time as the obligation to deliver tax benefits is relieved. The Company does not anticipate any credit recaptures will be required in connection with this arrangement.

The Company determined that this financing arrangement contains a VIE. The ongoing activities of the Tile Shop Investment Fund LLC – collecting and remitting interest and fees and NMTC compliance – were all considered in the initial design and are not expected to significantly affect economic performance throughout the life of the Tile Shop Investment Fund LLC. Management considered the contractual arrangements that obligate the Company to deliver tax benefits and provide various other guarantees to the structure; the investors lack of a material interest in the underlying economics of the project; and the fact that the Company is obligated to absorb losses of the Investment Fund. The Company concluded that it is the primary beneficiary of the VIE and consolidated the Tile Shop Investment Fund LLC, as a VIE, in accordance with the accounting standards for consolidation. In 2013, the investors' contributions, of \$5.6 million, net of syndication fees, were included in cash, restricted cash, other accrued liabilities and other long-term liabilities in the Consolidated Balance Sheet. The Company incurred \$1.2 million of syndication fees in connection with this transaction which were classified as other current assets and other non-current assets in the Consolidated Balance Sheet. The Company is recognizing the benefit of this net \$4.4 million contribution over the seven-year compliance period as it is being earned through the on-going compliance with the conditions of the NMTC program. As of June 30, 2018, the balance of the contribution liability was \$1.4 million, of which \$0.7 million is classified as other accrued liabilities on the Consolidated Balance Sheet and \$0.7 million is classified as other long-term liabilities on the Consolidated Balance Sheet.

#### Note 11: Commitments and Contingencies

The Company is a nominal defendant in three actions brought derivatively on behalf of the Company by three shareholders in 2015. The plaintiffs allege that the defendant-directors and/or officers breached their fiduciary duties by failing to adopt adequate internal controls for the Company, by approving false and misleading statements issued by the Company, by causing the Company to violate generally accepted accounting principles and SEC regulations, and by permitting the Company's primary product to contain illegal amounts of lead. The complaints also allege claims for insider trading and/or unjust enrichment. The Company moved to dismiss the actions, or in the alternative, to stay the actions. Before the motions were decided, the parties entered into settlement discussions. As of April 11, 2018, the parties entered into a Stipulation of Settlement to resolve all claims in the three actions, which is subject to the approval of the Delaware Court of Chancery. Under the terms of settlement, the Board of Directors will adopt, and the Company will implement, certain changes to its policies and practices that address related person transactions, insider trading, compliance, and ethics. The Stipulation of Settlement also provides that the Company will be liable to pay to plaintiffs and their counsel such amount of attorneys' fees, expenses, and incentive awards as the Court might award to them. The plaintiffs have formally requested that the Court award them attorneys' fees and expenses in the amount of \$1.7 million and an incentive award of \$5,000 for each of

Table of Contents

Tile Shop Holdings, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

the two plaintiffs. The Company intends to oppose the requested amount of attorneys' fees and expenses as being excessive. The Court is scheduled to hold a hearing on final approval of the settlement on August 23, 2018.

By letter dated May 19, 2016, a shareholder of the Company demanded that the Board of Directors investigate alleged breaches of fiduciary duty related to the same matters described above and take action against certain present and former officers and directors of the Company. The Board of Directors has appointed a committee of two independent directors to investigate and evaluate the matters raised in the demand letter, and to recommend to the Company's Board of Directors what actions, if any, should be taken by the Company with respect to the matters raised in the demand letter. The settlement of the three derivative actions described in the preceding paragraph, if approved by the Delaware Court of Chancery, will resolve this shareholder demand.

Based on the terms of the Settlement and range of potential award of attorneys' fees and expenses, the Company does not believe the amount of losses resulting from the derivative actions and demands will have a material impact on its financial statements.

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

Note 12: Related Party Transactions

On July 9, 2018 Fumitake Nishi, the brother-in-law of our interim CEO Robert Rucker and a former Company employee, informed us he had reacquired a majority of the equity of one of our key vendors, Nanyang Helin Stone Co. Ltd ("Nanyang"). Nanyang supplies us with natural stone products including hand-crafted mosaics, listellos and other accessories. During 2016, 2017 and the first six months of 2018, we purchased approximately \$8.4 million, \$12.8 million and \$5.7 million, respectively, of products from Nanyang. Mr. Nishi's employment in our Company was terminated on January 1, 2014 as a result of several violations of our code of business conduct and ethics policy. Certain of those violations involved his undisclosed ownership of Nanyang at that time.

Management and the Audit Committee have evaluated the relationship and determined that it would be in the Company's best interests to continue purchasing products from Nanyang. The Company believes Nanyang provides an important combination of quality, product availability and pricing, and relying solely on other vendors to supply similar product to the Company would not be in the Company's best interests. The Company and the Committee will review future purchases from Nanyang and compare the pricing for products purchased from Nanyang to the pricing of same or similar products purchased from unrelated vendors.

Note 13: Subsequent Events

On July 19, 2018, the Company declared a \$0.05 dividend to stockholders of record as of the close of business on July 30, 2018. The dividend will be paid on August 10, 2018.



Table of Contents

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2017 and our consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains “forward-looking statements” that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or Exchange Act. Forward-looking statements are often identified by the use of words such as, but not limited to, “anticipate,” “believe,” “can,” “continue,” “could,” “depend,” “estimate,” “expect,” “intend,” “may,” “might,” “plan,” “project,” “target,” “will,” “will likely result,” “would,” and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, unexpected delays or expenses related to maintaining or renovating existing stores, changes to our promotional strategy changes to economic or market conditions and customer preferences, disruptions in our supply chain, or inventory management, changes to our product assortment, competitive factors, increases to interest rates or other impacts on our ability to obtain or maintain financing, unanticipated expenses related to operating as a public company including but not limited to litigation-related expenses, and those factors disclosed in the section captioned “Risk Factors” in our Annual Report for the fiscal year ended December 31, 2017, filed with the Securities and Exchange Commission. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview and Recent Trends

We are a specialty retailer of natural stone and man-made tiles, setting and maintenance materials, and related accessories in the United States. We offer a wide selection of products, attractive prices, and exceptional customer service in an extensive showroom setting. As of June 30, 2018, we operated 140 stores in 31 states and the District of Columbia, with an average size of 20,200 square feet. We also sell our products on our website.

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

We believe that the highly-fragmented United States retail tile market provides us with a significant opportunity to expand our store base. We opened 2 new stores in the first six months of 2018, and opened 15 new stores during 2017. Between July 1, 2017 and June 30, 2018, we opened 10 new store locations. We do not plan to open any additional stores in 2018. We believe that there will continue to be additional expansion opportunities in the United States and Canada. We expect store base growth will drive productivity and operational efficiencies. Our growth plans also require us to maintain significant inventory on-hand in order to fulfill transactions at these new locations.

For the three months ended June 30, 2018 and 2017, we reported net sales of \$92.9 million and \$89.5 million, respectively. The increase in sales for the three months ended June 30, 2018 compared to the three months ended June 30, 2017 was primarily due to net sales of \$5.0 million from stores not included in the comparable store base, partially offset by a decline in comparable stores sales of 1.8%, or \$1.6 million. For the six months ended June 30, 2018 and 2017, we reported net sales of \$184.0 million and \$181.6 million, respectively. The increase in sales for the six months ended June 30, 2018 compared to the six months ended June 30, 2017 was primarily due to net sales of \$10.4 million from stores not included in the comparable store base, partially offset by a decline in comparable store sales of 4.4%, or \$7.9 million.

The decrease in sales at comparable stores for the three and six months ended June 30, 2018 was primarily the result of weaker store traffic due in part to our shift in promotional strategy.

Table of Contents

The table below sets forth information about our comparable store sales (decline) and growth for the three and six months ended June 30, 2018 and 2017.

	For the three months ended June 30,		For the six months ended June 30,	
	2018	2017	2018	2017
Comparable store sales (decline) growth	(1.8)%	0.5 %	(4.4)%	2.7 %

For the three months ended June 30, 2018 and 2017, we reported gross profit of \$65.3 million and \$62.3 million, respectively. The gross margin rate for the three months ended June 30, 2018 and 2017 was 70.3% and 69.7%, respectively. For the six months ended June 30, 2018 and 2017, we reported gross profit of \$129.4 million and \$127.1 million, respectively. The gross margin rate for the six months ended June 30, 2018 and 2017 was 70.3% and 70.0%, respectively. The improvement in gross profit dollars for the three and six months ended June 30, 2018 is attributable to an increase in sales combined with an increase in the gross margin rate. The increase in the gross margin rate is primarily due to decreased promotional activity.

For the three months ended June 30, 2018 and 2017, we reported income from operations of \$7.4 million and \$11.6 million, respectively. For the six months ended June 30, 2018 and 2017, we reported income from operations of \$13.6 million and \$25.1 million, respectively. The decrease in income from operations was primarily driven by investments made in store compensation, regional leadership, website design and customer relationship management capabilities combined with an increase in occupancy costs from new stores that have opened since July 1, 2017.

Inventory increased by \$12.1 million from \$88.3 million on March 31, 2018 to \$100.4 million on June 30, 2018. The increase was attributable to new products added to our assortment during the quarter.

Long term debt increased \$4.3 million from \$25.2 million on March 31, 2018 to \$29.5 million on June 30, 2018. The increase was attributable to the expansion of our product assortment resulting in an increase in inventory and capital investments associated with store remodels and merchandising.

Net cash provided by operating activities was \$19.3 million and \$34.8 million for the six months ended June 30, 2018 and 2017, respectively, which was used to fund operations, inventory purchases, store remodel and merchandising

investments, and dividends. We expect to continue to fund our capital expenditures and daily operations from our operating cash flows. As of June 30, 2018, we had cash of \$9.9 million and working capital of \$55.9 million compared with cash of \$6.6 million and working capital of \$43.5 million at December 31, 2017.

#### Key Components of our Consolidated Statements of Income

**Net Sales** Net sales represents total charges to customers, net of returns, and includes freight charged to customers. We recognize sales at the time that the customer takes control of the merchandise or final delivery of the product has occurred. We are required to charge and collect sales and other taxes on sales to our customers and remit these taxes back to government authorities. Total revenues do not include sales tax because we are a pass-through conduit for collecting and remitting sales tax. Sales are reduced by a reserve for anticipated sales returns that we estimate based on historical returns.

**Comparable store sales growth** is a percentage change in sales of comparable stores period-over-period. A store is considered comparable on the first day of the 13th full month of operation. When a store is relocated, it is excluded from the comparable stores sales growth calculation. Comparable store sales growth amounts include total charges to customers less any actual returns. We include the change in allowance for anticipated sales returns applicable to comparable stores in the comparable store sales calculation.

**Cost of Sales** Cost of sales consists primarily of material costs, freight, customs and duties fees, and storage and delivery of product to the customers, as well as physical inventory losses and costs associated with manufacturing of setting and maintenance materials.

**Selling, General, and Administrative Expenses** Selling, general, and administrative expenses consists primarily of compensation costs, occupancy, utilities, maintenance costs, advertising costs, shipping and transportation expenses to move inventory from our distribution centers to our stores, depreciation and amortization.

**Pre-opening Costs** Our pre-opening costs are those typically associated with the opening of a new store and generally include rent expense, compensation costs and promotional costs. We expense pre-opening costs as incurred and include these costs in selling, general, and administrative expenses.

**Provision for Income Taxes** We are subject to income tax in the United States as well as other tax jurisdictions in which we conduct business.



Table of Contents

## Non-GAAP Measure

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

We believe that this non-GAAP measure of financial results provides useful information to management and investors regarding certain financial and business trends relating to our financial condition and results of operations. Our management uses this non-GAAP measure 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. This measure is used in monthly financial reports prepared for management and our Board of Directors. We believe that the use of this non-GAAP financial measure provides an additional tool for investors to use in evaluating ongoing operating results and trends and in comparing our financial performance with other specialty retailers, many of which present a similar non-GAAP financial measure to investors.

The reconciliation of Adjusted EBITDA to net income for the three and six months ended June 30, 2018 and 2017 is as follows:

	(in thousands)					
	Three Months Ended					
	June 30,					
	2018	% of net	2017	% of net		
		sales(2)		sales(1)(2)		
Net income	\$ 4,958	5.3 %	\$ 7,723	8.6 %		
Interest expense	597	0.6 %	448	0.5 %		
Income taxes	1,924	2.1 %	3,491	3.9 %		
Depreciation & amortization	6,978	7.5 %	6,256	7.0 %		
Stock based compensation	598	0.6 %	928	1.0 %		
Adjusted EBITDA	\$ 15,055	16.2 %	\$ 18,846	21.1 %		

	(in thousands)		Six Months Ended		June 30,	
	2018	% of net sales	2017	% of net sales(1)		
Net income	\$ 8,969	4.9 %	\$ 15,732	8.7		%
Interest expense	1,151	0.6 %	933	0.5		%
Income taxes	3,505	1.9 %	8,566	4.7		%
Depreciation & amortization	13,978	7.6 %	12,592	6.9		%
Stock based compensation	1,215	0.7 %	1,770	1.0		%
Adjusted EBITDA	\$ 28,818	15.7 %	\$ 39,593	21.8		%

(1) In prior periods, the Company also adjusted for special charges, including shareholder and other litigation costs. The Company has recast the Adjusted EBITDA presentation for the three and six months ended June 30, 2017 to conform to the current presentation.

(2) Amounts may not foot due to rounding.

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

Table of Contents

## Results of Operations

Comparison of the three months ended June 30, 2018 to the three months ended June 30, 2017

	(in thousands)			
	2018	% of sales	2017	% of sales
Net sales	\$ 92,914		\$ 89,464	
Cost of sales	27,602	29.7 %	27,116	30.3 %
Gross profit	65,312	70.3 %	62,348	69.7 %
Selling, general and administrative expenses	57,870	62.3 %	50,748	56.7 %
Income from operations	7,442	8.0 %	11,600	13.0 %
Interest expense	(597)	(0.6) %	(448)	(0.5) %
Other income	37	0.0 %	62	0.1 %
Income before income taxes	6,882	7.4 %	11,214	12.5 %
Provision for income taxes	(1,924)	(2.1) %	(3,491)	(3.9) %
Net income	\$ 4,958	5.3 %	\$ 7,723	8.6 %

**Net Sales** Net sales for the second quarter of 2018 increased \$3.4 million, or 3.9%, compared with the second quarter of 2017, primarily due to a \$5.0 million increase in net sales from stores not included in the comparable store base, partially offset by a \$1.6 million decrease in net sales generated by comparable stores. The decrease in sales at comparable stores for the three months ended June 30, 2018 was due to weaker store traffic due in part to our shift in promotional strategy.

**Gross Profit** Gross profit for the second quarter of 2018 increased \$3.0 million, or 4.8%, compared with the second quarter of 2017 due to an increase in net sales and the gross margin rate. The gross margin rate was 70.3% and 69.7% for the second quarter of 2018 and 2017, respectively. The improvement in the gross margin rate was primarily due to decreased promotional activity.

**Selling, General, and Administrative Expenses** Selling, general, and administrative expenses for the second quarter of 2018 increased \$7.1 million, or 14.0%, compared with the second quarter of 2017. The \$7.1 million increase in selling, general, and administrative expenses was driven primarily by costs associated with opening and operating 10 new stores during the period from July 1, 2017 through June 30, 2018, investments in store and warehouse staff compensation, and the addition of regional sales leader positions. Included in the selling, general, and administrative



expenses increase during the second quarter of 2018 was \$2.0 million of planned strategic investments in store compensation, regional sales leadership, website design, and customer relationship management capabilities.

**Pre-opening Costs** During the three months ended June 30, 2018 and 2017, we incurred pre-opening costs of \$0.0 million and \$0.5 million, respectively.

**Interest Expense** Interest expense was \$0.6 million and \$0.4 million for the second quarter of 2018 and 2017, respectively. The increase was due to higher interest rates during the second quarter of 2018.

**Provision for Income Taxes** Income tax provision decreased \$1.6 million for the second quarter of 2018 compared with the second quarter of 2017 due to a decrease in income before income taxes, along with a decrease in our effective tax rate due to the Tax Act. Our effective tax rate for the three months ended June 30, 2018 and 2017 was 28.0% and 31.1%, respectively.

Table of Contents

Comparison of the six months ended June 30, 2018 to the six months ended June 30, 2017

	(in thousands)			
	2018	% of sales	2017	% of sales
Net sales	\$ 184,048		\$ 181,599	
Cost of sales	54,698	29.7 %	54,506	30.0 %
Gross profit	129,350	70.3 %	127,093	70.0 %
Selling, general and administrative expenses	115,797	62.9 %	101,960	56.1 %
Income from operations	13,553	7.4 %	25,133	13.8 %
Interest expense	(1,151)	(0.6) %	(933)	(0.5) %
Other income (expense)	72	0.0 %	98	0.1 %
Income before income taxes	12,474	6.8 %	24,298	13.4 %
Provision for income taxes	(3,505)	(1.9) %	(8,566)	(4.7) %
Net income	\$ 8,969	4.9 %	\$ 15,732	8.7 %

**Net Sales** Net sales for the six months ended June 30, 2018 increased \$2.4 million, or 1.3%, compared with the six months ended June 30, 2017, primarily due to a \$7.9 million decrease in net sales generated by comparable stores. The decrease in sales at comparable stores for the six months ended June 30, 2018 was due to weaker store traffic due in part to our shift in promotional strategy.

**Gross Profit** Gross profit for the six months ended June 30, 2018 increased \$2.3 million, or 1.8%, compared with the six months ended June 30, 2017 primarily due to an increase in net sales and an increase in the gross margin rate. The gross margin rate was 70.3% and 70.0% for the six months ended June 30, 2018 and 2017, respectively. The improvement in the gross margin rate was primarily due to decreased promotional activity.

**Selling, General, and Administrative Expenses** Selling, general, and administrative expenses for the six months ended June 30, 2018 increased \$13.8 million, or 13.6%, compared with the six months ended June 30, 2017. The \$13.8 million increase in selling, general, and administrative expenses was driven primarily by costs associated with opening and operating 10 new stores during the period from July 1, 2017 through June 30, 2018, investments in store and warehouse staff compensation, and the addition of regional sales leader positions. Included in the selling, general, and administrative expenses increase during the six months ended June 30, 2018 was approximately \$4.0 million of planned strategic investments in store compensation, regional sales leadership, website design, and customer relationship management capabilities.

Pre-opening Costs During the six months ended June 30, 2018 and 2017, we incurred pre-opening costs of \$0.1 million and \$0.8 million, respectively.

Interest Expense Interest expense was \$1.2 million and \$0.9 million for the six months ended June 30, 2018 and 2017, respectively. The increase was due to higher interest rates and a higher debt balance during the six months ended June 30, 2018.

Provision for Income Taxes Income tax provision decreased \$5.1 million for the six months ended June 30, 2018 compared with the six months ended June 30, 2017 due to a decrease in income before income taxes, along with a decrease in our effective tax rate due to the Tax Act. Our effective tax rate for the six months ended June 30, 2018 and 2017 was 28.1% and 35.3%, respectively.

### Liquidity and Capital Resources

Our principal uses of liquidity have been investments in working capital and capital expenditures. Our principal sources of liquidity are \$9.9 million of cash and cash equivalents at June 30, 2018, our cash flow from operations, and borrowings available under our credit facility. We expect to use this liquidity for opening new stores, purchasing additional merchandise inventory, maintaining our existing stores, reducing outstanding debt, paying dividends to our shareholders and general corporate purposes.

On June 2, 2015, we and our operating subsidiary, The Tile Shop, LLC, entered into a credit agreement with Fifth Third Bank, Bank of America, N.A., and Huntington National Bank (as amended, the "Credit Agreement"). The Credit Agreement was most recently amended on April 5, 2018 to adjust the consolidated fixed charge coverage ratio covenant to a minimum of 1.35:1.00 and revise the consolidated total rent adjusted leverage ratio covenant to a maximum of 4.00:1.00.

The Credit Agreement provides us with a \$125.0 million senior secured credit facility, comprised of a five-year \$50.0 million term loan and a \$75.0 million revolving line of credit. Borrowings outstanding consisted of \$7.0 million on the term loan and \$22.5 million

Table of Contents

on the revolving line of credit as of June 30, 2018. There was \$52.5 million available for borrowing on the revolving line of credit as of June 30, 2018, which may be used to support our growth and for working capital purposes.

Borrowings pursuant to the Credit Agreement bear interest at either a base rate or a LIBOR-based rate, at our option. The LIBOR-based rate will range from LIBOR plus 1.50% to 2.00%, depending on our leverage ratio. The base rate is equal to the greatest of: (a) the Federal funds rate plus 0.50%, (b) the Fifth Third Bank “prime rate,” and (c) the Eurodollar rate plus 1.00%, in each case plus 0.50% to 1.00% depending on our leverage ratio. At June 30, 2018 the base interest rate was 5.75% and the LIBOR-based interest rate was 3.84%.

The term loan requires quarterly principal payments of \$2.5 million for the quarters ended September 30, 2018 through March 31, 2020. We can elect to prepay the term loan without incurring a penalty.

The Credit Agreement is secured by virtually all of our assets, including but not limited to, inventory, receivables, equipment and real property. The Credit Agreement contains customary events of default, conditions to borrowings, and restrictive covenants, including restrictions on our ability to dispose of assets, make acquisitions, incur additional debt, incur liens, make investments, or enter into transactions with affiliates on other than terms that could be obtained in an arm’s length transaction. The Credit Agreement also includes financial and other covenants, including covenants to maintain certain fixed charge coverage ratios and rent adjusted leverage ratios. We were in compliance with the covenants as of June 30, 2018. We intend to make principal payments due in future periods using cash from operations.

We have standby letters of credit outstanding related to our workers compensation and medical insurance policies. As of June 30, 2018 and 2017, the standby letters of credit totaled \$1.1 million.

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

Capital Expenditures

## Edgar Filing: Stone Harbor Emerging Markets Income Fund - Form 40-17G

Capital expenditures were \$13.1 million and \$20.0 million for the six months ended June 30, 2018 and 2017, respectively. The decrease in capital expenditures is primarily due to the decelerated pace of new store openings. We opened 2 and 7 new stores during the six months ended June 30, 2018 and 2017, respectively. During the six months ended June 30, 2018, capital expenditures primarily consisted of remodels for existing store investments and information technology investments.

### Cash flows

The following table summarizes our cash flow data for the six months ended June 30, 2018 and 2017.

	(in thousands)	
	Six Months Ended	
	June 30,	
	2018	2017
Net cash provided by operating activities	\$ 19,276	\$ 34,828
Net cash used in investing activities	(13,134)	(20,000)
Net cash used in financing activities	(2,868)	(14,923)

### Operating activities

Net cash provided by operating activities during the six months ended June 30, 2018 was \$19.3 million compared with \$34.8 million during the six months ended June 30, 2017. The decrease is attributable to a decrease in net income, along with an increase in inventory.

### Investing activities

Net cash used in investing activities totaled \$13.1 million for the six months ended June 30, 2018 compared with \$20.0 million for the six months ended June 30, 2017. Net cash used in investing activities in each period was primarily for capital purchases of store fixtures, equipment, building improvements and leasehold improvements for stores opened or remodeled, asset additions in our distribution and manufacturing facilities, information technology infrastructure, a new enterprise resource planning system, and general corporate information technology assets.



## Table of Contents

### Financing activities

Net cash used in financing activities was \$2.9 million for the six months ended June 30, 2018 compared with \$14.9 million for the six months ended June 30, 2017. Net cash used in financing activities during the six months ended June 30, 2018 included \$32.6 million in payments of long-term debt and capital lease obligations and \$5.2 million in dividends paid to stockholders, offset by advances on the line of credit of \$35.0 million.

Cash and cash equivalents totaled \$9.9 million at June 30, 2018 compared with \$6.6 million at December 31, 2017. Working capital was \$55.9 million at June 30, 2018 compared with \$43.5 million at December 31, 2017.

### Off-Balance Sheet Arrangements

As of June 30, 2018 and December 31, 2017, we did not have any “off-balance sheet arrangements” (as such term is defined in Item 303 of Regulation S-K) that could have a current or future effect on our financial condition, changes in financial condition, net sales or expenses, results of operations, liquidity, capital expenditures or capital resources.

### Contractual Arrangements

As of June 30, 2018, there were no material changes to our contractual obligations outside the ordinary course of business.

### Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued a final standard on revenue from contracts with customers. This new standard introduces a comprehensive revenue recognition model that requires a company to recognize revenue to depict the transfer of goods or services to a customer at an amount that reflects the consideration it expects to receive in exchange for those goods or services. In 2016, the FASB issued several amendments to the standard. We adopted this standard as of January 1, 2018 using the modified retrospective transition method. See Note 2 in Item 1, Notes to Consolidated Financial Statements in this Form 10-Q for further details.

In November 2016, the FASB issued new guidance on restricted cash on the statement of cash flows. The new guidance requires the classification and presentation of changes in restricted cash and cash equivalents in the statement of cash flows. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning and ending balances shown in the statement of cash flows. We adopted the new standard as of March 31, 2018 using the retrospective transition method. Our restricted cash balance was \$0.8 million as of June 30, 2018. Upon adopting the new standard, we no longer present the release of restricted cash as a financing cash inflow. Instead, restricted cash and long-term restricted cash balances will be included in the beginning and ending cash, cash equivalents and restricted cash balances in the statement of cash flows. In connection with the adoption of this standard, \$6.0 million received from restricted cash accounts during six months ended June 30, 2017 that was previously presented as a financing cash inflow was reclassified to cash, cash equivalents and restricted cash in the statement of cash flows.

#### Accounting Pronouncements Not Yet Adopted

In February 2016, the FASB issued a standard that primarily requires organizations that lease assets to recognize the rights and obligations created by those leases on the consolidated balance sheet. The standard is effective for fiscal year 2019, with early adoption permitted. We expect the primary impact on our consolidated balance sheets upon adoption will be the recognition, on a discounted basis, of our minimum commitments under non-cancelable operating leases resulting in the recording of right of use assets and lease obligations. Our minimum commitments under non-cancelable operating leases are disclosed in Note 5 to the Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. We have identified our lease management system and are in the process of identifying and evaluating the applicable leases. We are currently assessing the effect the new standard will have on our consolidated financial statements.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in our primary risk exposures or management of market risks from those disclosed in our Annual Report Form 10-K for the fiscal year ended December 31, 2017.



Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We have established disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934, as amended, (the “Exchange Act”), is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that information relating to the Company is accumulated and communicated to management, including our principal officers as appropriate to allow timely decisions regarding required disclosure. Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2018 and have concluded that such disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

Changes in Internal Control over Financial Reporting

No changes to our internal control over financial reporting occurred during the quarter ended June 30, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act).

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is a nominal defendant in three actions brought derivatively on behalf of the Company by three shareholders in 2015. The plaintiffs allege that the defendant-directors and/or officers breached their fiduciary duties by failing to adopt adequate internal controls for the Company, by approving false and misleading statements issued by the Company, by causing the Company to violate generally accepted accounting principles and SEC regulations, and by permitting the Company’s primary product to contain illegal amounts of lead. The complaints also allege claims for insider trading and/or unjust enrichment. The Company moved to dismiss the actions, or in the alternative, to stay the actions. Before the motions were decided, the parties entered into settlement discussions. As of April 11, 2018, the parties entered into a Stipulation of Settlement to resolve all claims in the three actions, which is subject to the approval of the Delaware Court of Chancery. Under the terms of settlement, the Board of Directors will adopt, and the Company will implement, certain changes to its policies and practices that address related person transactions,

insider trading, compliance, and ethics. The Stipulation of Settlement also provides that the Company will be liable to pay to plaintiffs and their counsel such amount of attorneys' fees, expenses, and incentive awards as the Court might award to them. The plaintiffs have formally requested that the Court award them attorneys' fees and expenses in the amount of \$1.7 million and an incentive award of \$5,000 for each of the two plaintiffs. The Company intends to oppose the requested amount of attorneys' fees and expenses as being excessive. The Court is scheduled to hold a hearing on final approval of the settlement on August 23, 2018.

By letter dated May 19, 2016, a shareholder of the Company demanded that the Board of Directors investigate alleged breaches of fiduciary duty related to the same matters described above and take action against certain present and former officers and directors of the Company. The Board of Directors has appointed a committee of two independent directors to investigate and evaluate the matters raised in the demand letter, and to recommend to the Company's Board of Directors what actions, if any, should be taken by the Company with respect to the matters raised in the demand letter. The settlement of the three derivative actions described in the preceding paragraph, if approved by the Delaware Court of Chancery, will resolve this shareholder demand.

Based on the terms of the Settlement and range of potential award of attorneys' fees and expenses, the Company does not believe the amount of losses resulting from the derivative actions and demands will have a material impact on its financial statements.

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

#### ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2017.

Table of Contents

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

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Program	Maximum Number of Shares that May Yet be Purchased Under Plans or Programs
April 1, 2018 - April 30, 2018	9,358	(1) \$ 0.60 (1)	-	-
May 1, 2018 - May 31, 2018	3,658	(2) 6.74 (2)	-	-
June 1, 2018 - June 30, 2018	-	-	-	-
	13,016	\$ 2.32	-	-

(1) A total of 931 shares were withheld by the Company to satisfy tax withholding obligations due upon the vesting of restricted stock grants, as allowed by the 2012 Omnibus Incentive Plan. The Company did not pay cash to repurchase these shares, nor were these repurchases part of a publicly announced plan or program. The remaining 8,427 shares were repurchased by the Company pursuant to the terms of the underlying restricted stock agreements, as allowed by the 2012 Omnibus Incentive Plan. The Company paid \$0.0001 per share, the par value, to repurchase these shares. These repurchases were not part of a publicly announced plan or program.

(2) These shares were withheld by the Company to satisfy tax withholding obligations due upon the vesting of restricted stock grants, as allowed by the 2012 Omnibus Incentive Plan. The Company did not pay cash to repurchase these shares, nor were these repurchases part of a publicly announced plan or program.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

## ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

#### ITEM 5. OTHER INFORMATION

On July 9, 2018 Fumitake Nishi, the brother-in-law of our interim CEO Robert Rucker and a former Company employee, informed us he had reacquired a majority of the equity of one of our key vendors, Nanyang Helin Stone Co. Ltd (“Nanyang”). Nanyang supplies us with natural stone products including hand-crafted mosaics, listellos and other accessories. During 2016, 2017 and the first six months of 2018, we purchased approximately \$8.4 million, \$12.8 million and \$5.7 million, respectively, of products from Nanyang. Mr. Nishi’s employment in our Company was terminated on January 1, 2014 as a result of several violations of our code of business conduct and ethics policy. Certain of those violations involved his undisclosed ownership of Nanyang at that time.

Management and the Audit Committee have evaluated the relationship and determined that it would be in the Company’s best interests to continue purchasing products from Nanyang. The Company believes Nanyang provides an important combination of quality, product availability and pricing, and relying solely on other vendors to supply similar product to the Company would not be in the Company’s best interests. The Company and the Committee will review future purchases from Nanyang and compare the pricing for products purchased from Nanyang to the pricing of same or similar products purchased from unrelated vendors.

Table of Contents

ITEM 6. EXHIBITS

Exhibits

- 3.1 Certificate of Incorporation of Tile Shop Holdings, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Registration Statement on Form S-4 (Reg. No. 333-182482) filed with the Securities and Exchange Commission on July 2, 2012).
- 3.2 By-Laws of Tile Shop Holdings, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form S-4 (Reg. No. 333-182482) filed with the Securities and Exchange Commission on July 2, 2012).
- 10.1 Fourth Amendment to Credit Agreement, dated April 5, 2018, among The Tile Shop, LLC, Tile Shop Holdings, Inc., Fifth Third Bank, and the other parties named therein (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on April 6, 2018).
- 31.1\* Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
- 31.2\* Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
- 32.1\*\* Certifications of Chief Executive Officer Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
- 32.2\*\* Certifications of Chief Financial Officer Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.
- 101.INS\* XBRL Instance Document.
- 101.SCH\* XBRL Taxonomy Extension Schema Document.
- 101.CAL\* XBRL Taxonomy Extension Calculation Linkbase Document.
- 101.DEF\* XBRL Taxonomy Extension Definition Linkbase Document.
- 101.LAB\* XBRL Taxonomy Extension Label Linkbase Document.
- 101.PRE\* XBRL Taxonomy Extension Presentation Linkbase Document.

\* Filed herewith

\*\* Furnished herewith

Table of Contents

SIGNATURES

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

TILE SHOP HOLDINGS, INC.

Dated: August 1, 2018 By: /s/ ROBERT A. RUCKER  
Robert A. Rucker  
Chief Executive Officer

Dated: August 1, 2018 By: /s/ KIRK L. GEADELMANN  
Kirk L. Geadelmann  
Chief Financial Officer