

TANDY LEATHER FACTORY INC  
Form 10-Q  
May 16, 2016

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2016

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-12368

TANDY LEATHER FACTORY, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

75-2543540  
(I.R.S. Employer Identification No.)

1900 Southeast Loop 820, Fort Worth, Texas 76140  
(Address of principal executive offices) (Zip code)

(817) 872-3200  
(Registrant's telephone number, including area code)

\_\_\_\_\_  
(Former name, former address and former fiscal year, if changed since last report)

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

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one): Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [X]

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

| Class                                      | Shares outstanding as of May 10, 2016 |
|--|---------------------------------------|
| Common Stock, par value \$0.0024 per share | 9,272,012                             |

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TANDY LEATHER FACTORY, INC.

FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2016

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements.

Tandy Leather Factory, Inc.  
Consolidated Balance Sheets

|   | March 31,<br>2016<br>(unaudited) | December<br>31,<br>2015<br>(audited) |
|---|----------------------------------|--------------------------------------|
| <b>ASSETS</b>   |                                  |                                      |
| <b>CURRENT ASSETS:</b>  |                                  |                                      |
| Cash  | \$11,444,262                     | \$10,962,615                         |
| Accounts receivable-trade, net of allowance for doubtful accounts<br>of \$1,677 and \$1,746 in 2016 and 2015, respectively    | 682,580                          | 553,206                              |
| Inventory   | 33,632,302                       | 33,584,539                           |
| Prepaid income taxes  | 188,430                          | 549,277                              |
| Deferred income taxes   | 328,048                          | 326,830                              |
| Prepaid expenses  | 1,627,169                        | 1,514,887                            |
| Other current assets  | 146,273                          | 70,197                               |
| Total current assets  | 48,049,064                       | 47,561,551                           |
| PROPERTY AND EQUIPMENT, at cost   | 24,548,702                       | 23,992,208                           |
| Less accumulated depreciation and amortization  | (8,650,964)                      | (8,297,155)                          |
|   | 15,897,738                       | 15,695,053                           |
| GOODWILL  | 959,784                          | 953,356                              |
| OTHER INTANGIBLES, net of accumulated amortization of approximately<br>\$706,000 and \$702,000 in 2016 and 2015, respectively | 23,421                           | 27,282                               |
| OTHER assets  | 329,838                          | 329,684                              |
| <b>TOTAL ASSETS</b>   | <b>\$65,259,845</b>              | <b>\$64,566,926</b>                  |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                  |                                      |
| <b>CURRENT LIABILITIES:</b>   |                                  |                                      |
| Accounts payable-trade  | \$1,920,311                      | \$1,983,376                          |
| Accrued expenses and other liabilities  | 4,573,776                        | 6,045,552                            |
| Current maturities of capital lease obligations   | 72,686                           | 72,686                               |
| Current maturities of long-term debt  | 822,653                          | 231,952                              |
| Total current liabilities   | 7,389,426                        | 8,333,566                            |
| DEFERRED INCOME TAXES   | 1,735,450                        | 1,702,515                            |
| LONG-TERM DEBT, net of current maturities   | 5,758,571                        | 3,479,273                            |
| CAPITAL LEASE OBLIGATIONS, net of current maturities  | 72,688                           | 79,396                               |
| COMMITMENTS AND CONTINGENCIES   |                                  | -                                    |
| <b>STOCKHOLDERS' EQUITY:</b>  |                                  |                                      |
| Preferred stock, \$0.10 par value; 20,000,000 shares authorized;  |                                  |                                      |

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|   |              |              |
|---|--------------|--------------|
| none issued or outstanding; attributes to be determined on issuance   | -            | -            |
| Common stock, \$0.0024 par value; 25,000,000 shares authorized;<br>11,309,326 and 11,275,641 shares issued at 2016 and 2015,<br>respectively; |              |              |
| 9,382,555 and 9,753,293 shares outstanding at 2016 and 2015,<br>respectively  | 27,142       | 27,062       |
| Paid-in capital   | 6,212,171    | 6,168,489    |
| Retained earnings   | 54,588,231   | 53,067,234   |
| Treasury stock at cost (1,926,771 and 1,522,348 shares at 2016 and 2015,<br>respectively)   | (9,473,670)  | (6,602,930)  |
| Accumulated other comprehensive income  | (1,050,164)  | (1,687,679)  |
| Total stockholders' equity  | 50,303,710   | 50,972,176   |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY  | \$65,259,845 | \$64,566,926 |

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

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Tandy Leather Factory, Inc.  
Consolidated Statements of Income  
(Unaudited)  
For the Three Months Ended March 31, 2016 and 2015

|  | 2016         | 2015         |
|--|--------------|--------------|
| NET SALES                                      | \$20,672,227 | \$20,788,764 |
| COST OF SALES                                  | 8,019,481    | 8,205,836    |
| Gross profit                                   | 12,652,746   | 12,582,928   |
| OPERATING EXPENSES                             | 10,289,956   | 10,194,047   |
| INCOME FROM OPERATIONS                         | 2,362,790    | 2,388,881    |
| OTHER (INCOME) EXPENSE:                        |              |              |
| Interest expense                               | 23,429       | 44,163       |
| Other, net                                     | 39           | (19,873)     |
| Total other (income) expense                   | 23,468       | 24,290       |
| INCOME BEFORE INCOME TAXES                     | 2,339,322    | 2,364,591    |
| PROVISION FOR INCOME TAXES                     | 818,325      | 920,184      |
| NET INCOME                                     | \$1,520,997  | \$1,444,407  |
| NET INCOME PER COMMON SHARE:                   |              |              |
| BASIC  | \$0.16       | \$0.14       |
| DILUTED  | \$0.16       | \$0.14       |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING: |              |              |
| BASIC  | 9,698,951    | 10,211,333   |
| DILUTED  | 9,718,453    | 10,241,096   |

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



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Tandy Leather Factory, Inc.  
Consolidated Statements of Comprehensive Income  
(Unaudited)  
For the Three Months Ended March 31, 2016 and 2015

|  | 2016        | 2015        |
|--|-------------|-------------|
| NET INCOME   | \$1,520,997 | \$1,444,407 |
| Foreign currency translation adjustments, net of tax | 637,515     | (644,456)   |
| COMPREHENSIVE INCOME                                 | \$2,158,512 | \$799,951   |

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



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Tandy Leather Factory, Inc.  
Consolidated Statements of Cash Flows  
(Unaudited)  
For the Three Months Ended March 31, 2016 and 2015

|   | 2016           | 2015             |
|---|----------------|------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                |                  |
| Net income  | \$1,520,997    | \$1,444,407      |
| Adjustments to reconcile net income to net cash provided by operating activities: |                |                  |
| Depreciation and amortization   | 414,228        | 383,936          |
| (Gain) / loss on disposal or abandonment of assets                                | (12,023)       | 5,804            |
| Non-cash stock-based compensation   | 43,762         | 29,064           |
| Deferred income taxes   | 31,717         | 67,831           |
| Foreign currency translation  | 614,366        | (585,107)        |
| Net changes in assets and liabilities:  |                |                  |
| Accounts receivable-trade, net  | (129,374)      | (39,095)         |
| Inventory   | (47,763)       | 2,467,610        |
| Prepaid expenses  | (112,282)      | (123,481)        |
| Other current assets  | (76,076)       | 43,888           |
| Accounts payable-trade  | (63,065)       | 486,852          |
| Accrued expenses and other liabilities  | (1,471,776)    | (1,097,188)      |
| Income taxes payable  | 360,847        | 423,403          |
| Total adjustments   | (447,439)      | 2,063,517        |
| Net cash provided by operating activities   | 1,073,558      | 3,507,924        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                      |                |                  |
| Purchase of property and equipment  | (606,932)      | (677,444)        |
| Proceeds from sale of assets  | 22,625         | -                |
| Increase (decrease) in other assets   | (154)          | 2,344            |
| Net cash used in investing activities   | (584,461)      | (675,100)        |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                      |                |                  |
| Net decrease in revolving credit loans  | -              | (3,500,000)      |
| Proceeds from notes payable and long term debt                                    | 2,870,000      | -                |
| Payments on notes payable and long-term debt                                      | -              | (50,625)         |
| Payments on capital lease obligations   | (6,710)        | -                |
| Repurchase of common stock (treasury stock)                                       | (2,870,740)    | -                |
| Proceeds from issuance of common stock  | -              | 9,920            |
| Net cash used in financing activities   | (7,450)        | (3,540,705)      |
| <b>NET INCREASE (DECREASE) IN CASH</b>  | <b>481,647</b> | <b>(707,881)</b> |
| CASH, beginning of period   | 10,962,615     | 10,636,530       |
| CASH, end of period   | \$11,444,262   | \$9,928,649      |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>                         |                |                  |
| Interest paid during the period   | \$23,429       | \$44,163         |

|   |           |           |
|---|-----------|-----------|
| Income tax paid during the period, net of (refunds) | \$457,478 | \$379,690 |
|---|-----------|-----------|

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

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Tandy Leather Factory, Inc.  
 Consolidated Statements of Stockholders' Equity  
 (Unaudited)  
 For the Three Months Ended March 31, 2016 and 2015

|  | Number of<br>Shares | Par<br>Value | Paid-in<br>Capital | Treasury<br>Stock | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) | Total        |
|--|---------------------|--------------|--------------------|-------------------|----------------------|--|--------------|
| BALANCE, December<br>31, 2014            | 10,245,534          | \$26,984     | \$6,013,325        | \$(2,894,068)     | \$46,664,829         | \$(688,058)  | \$49,123,012 |
| Shares issued – stock<br>option exercise | 2,000               | 5            | 9,915              | -                 | -                    | -  | 9,920        |
| Stock-based<br>compensation              | 34,484              | 83           | 28,981             | -                 | -                    | -  | 29,064       |
| Net income                               | -                   | -            | -                  | -                 | 1,444,407            | -  | 1,444,407    |
| Translation adjustment                   | -                   | -            | -                  | -                 | -                    | (644,456)  | (644,456)    |
| BALANCE, March 31,<br>2015               | 10,282,018          | \$27,072     | \$6,052,221        | \$(2,894,068)     | \$48,109,236         | \$(1,332,514)  | \$49,961,947 |

|                               | Number of<br>Shares | Par<br>Value | Paid-in<br>Capital | Treasury<br>Stock | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) | Total        |
|-------------------------------|---------------------|--------------|--------------------|-------------------|----------------------|--|--------------|
| BALANCE, December<br>31, 2015 | 9,753,293           | \$27,062     | \$6,168,489        | \$(6,602,930)     | \$53,067,234         | \$(1,687,679)  | \$50,972,176 |
| Stock-based<br>compensation   | 33,685              | 80           | 43,682             | -                 | -                    | -  | 43,762       |
| Net income                    | -                   | -            | -                  | -                 | 1,520,997            | -  | 1,520,997    |
| Purchase of treasury<br>stock | (404,423)           | -            | -                  | (2,870,740)       | -                    | -  | (2,870,740)  |
| Translation adjustment        | -                   | -            | -                  | -                 | -                    | 637,515  | 637,515      |
| BALANCE, March 31,<br>2016    | 9,382,555           | \$27,142     | \$6,212,171        | \$(9,473,670)     | \$54,588,231         | \$(1,050,164)  | \$50,303,710 |

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



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TANDY LEATHER FACTORY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 1. BASIS OF PRESENTATION AND CERTAIN SIGNIFICANT ACCOUNTING POLICIES

In the opinion of management, the accompanying consolidated financial statements for Tandy Leather Factory, Inc. and its consolidated subsidiaries contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly its financial position as of March 31, 2016 and December 31, 2015, and its results of operations and cash flows for the three-month periods ended March 31, 2016 and 2015. Operating results for the three-month period ended March 31, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2015.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

**Inventory.** Inventory is stated at the lower of cost or market and is accounted for on the “first in, first out” method. Based on negotiations with vendors, title generally passes to us when merchandise is put on board. Merchandise to which we have title but have not yet received is recorded as inventory in transit. In addition, the value of inventory is periodically reduced for slow-moving or obsolete inventory based on management’s review of items on hand compared to their estimated future demand.

The components of inventory consist of the following:

|                                   | As of               |                      |
|-----------------------------------|---------------------|----------------------|
|                                   | March 31, 2016      | December 31,<br>2015 |
| <b>Inventory on hand:</b>         |                     |                      |
| Finished goods held for sale      | \$30,873,556        | \$30,487,764         |
| Raw materials and work in process | 1,227,891           | 1,284,567            |
| Inventory in transit              | 1,530,855           | 1,812,208            |
|                                   | <b>\$33,632,302</b> | <b>\$33,584,539</b>  |

**Goodwill and Other Intangibles.** Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a business combination. Goodwill is required to be evaluated for impairment on an annual basis, absent indicators of impairment during the interim. Application of the goodwill impairment test requires exercise of judgment, including the estimation of future cash flows, determination of appropriate discount rates and other important assumptions. Changes in these estimates and assumptions could materially affect the determination of fair value and/or goodwill impairment for each reporting unit.

A two-step process is used to test for goodwill impairment. The first phase screens for impairment, while the second phase (if necessary) measures the impairment. We have elected to perform the annual analysis during the fourth calendar quarter of each year. As of December 31, 2015, management determined that the present value of the discounted estimated future cash flows of the stores associated with the goodwill is sufficient to support their

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respective goodwill balances. No indicators of impairment were identified during the first quarter of 2016.

A summary of changes in our goodwill for the periods ended March 31, 2016 and 2015 is as follows:

|                              | Leather Factory | Tandy Leather | Total     |
|------------------------------|-----------------|---------------|-----------|
| Balance, January 1, 2015     | \$588,380       | \$383,406     | \$971,786 |
| Acquisitions and adjustments | -               | -             | -         |
| Foreign exchange gain/loss   | (9,695)         | -             | (9,695)   |
| Impairments                  | -               | -             | -         |
| Balance, March 31, 2015      | \$578,685       | \$383,406     | \$962,091 |
|                              | Leather Factory | Tandy Leather | Total     |
| Balance, January 1, 2016     | \$569,950       | \$383,406     | \$953,356 |
| Acquisitions and adjustments | -               | -             | -         |
| Foreign exchange gain/loss   | 6,428           | -             | 6,428     |
| Impairments                  | -               | -             | -         |
| Balance, March 31, 2016      | \$576,378       | \$383,406     | \$959,784 |

Other intangibles consist of the following:

|                           | As of March 31, 2016 |              |          | As of December 31, 2015 |              |          |
|---------------------------|----------------------|--------------|----------|-------------------------|--------------|----------|
|                           | Gross                | Accumulated  |          | Gross                   | Accumulated  |          |
|                           |                      | Amortization | Net      |                         | Amortization | Net      |
| Trademarks,<br>Copyrights | \$554,369            | \$544,698    | \$9,671  | \$554,369               | \$544,504    | \$9,865  |
| Non-Compete<br>Agreements | 174,665              | 160,915      | 13,750   | 174,665                 | 157,248      | 17,417   |
|                           | \$729,034            | \$705,613    | \$23,421 | \$729,034               | \$701,752    | \$27,282 |

We recorded amortization expense of \$3,861 during the first quarter of 2016 compared to \$11,278 during the first quarter of 2015. All of our intangible assets, other than goodwill, are subject to amortization under U.S. GAAP. Based on the current amount of intangible assets subject to amortization, the estimated amortization expense for each of the succeeding 5 years is as follows:

|            | Leather<br>Factory | Tandy<br>Leather | Total   |
|------------|--------------------|------------------|---------|
| 2016       | \$81               | \$2,500          | \$2,581 |
| 2017       | 90                 | 1,667            | 1,757   |
| 2018       | -                  | 1,417            | 1,417   |
| 2019       | -                  | 666              | 666     |
| 2020       | -                  | 666              | 666     |
| Thereafter | -                  | 6,334            | 6,334   |

Revenue Recognition. Our sales generally occur via two methods: (1) at the counter in our stores, and (2) shipment by common carrier. Sales at the counter are recorded and title passes as transactions occur. Otherwise, sales are recorded and title passes when the merchandise is shipped to the customer. Our shipping terms are FOB shipping point.

We offer an unconditional satisfaction guarantee to our customers and accept all product returns. Net sales represent gross sales less negotiated price allowances, product returns, and allowances for defective merchandise.



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Comprehensive Income (loss) and Accumulated Other Comprehensive Income (loss). Comprehensive income (loss) is defined as the change in equity during a period from transactions and other events and circumstances from non-stockholder sources and includes all changes in equity during a period except those resulting from investments by and dividends to stockholders. Our comprehensive income (loss) consists of our net income and foreign currency translation adjustments from our international operations.

Recent Accounting Pronouncements. In May 2014, the FASB issued ASU No. 2014-09, which amends ASC Topic 606, “Revenue from Contracts with Customers”. The amendments in this ASU are intended to provide a more robust framework for addressing revenue issues, improve comparability of revenue recognition practices and improve disclosure requirements. The amendments in this accounting standard update are effective for interim and annual reporting periods beginning after December 15, 2016. In April 2015, the FASB issued ASU No. 2015-24, Revenue from Contracts with Customers: Deferral of the Effective Date which proposed a deferral of the effective date by one year, and on July 7, 2015, the FASB decided to delay the effective date by one year. The deferral results in the new revenue standard being effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. We are therefore required to apply the new revenue guidance beginning in our 2018 interim and annual financial statements. This ASU can be adopted either retrospectively or as a cumulative-effect adjustment as of the date of adoption. Entities reporting under U.S. GAAP are not permitted to adopt this standard earlier than the original effective date for public entities (that is, no earlier than 2017 for calendar year-end entities.) We are evaluating what impact, if any, the adoption of this guidance will have on our consolidated financial condition, results of operations, cash flows or financial disclosures.

In June 2014, the FASB issued ASU No. 2014-12, which amends ASC Topic 718, “Compensation—Stock Compensation.” The guidance requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition and should not be reflected in the estimate of the grant-date fair value of the award. The guidance is effective for annual periods, and interim periods within those annual periods beginning after December 15, 2015. The guidance can be applied prospectively for all awards granted or modified after the effective date or retrospectively to all awards with performance targets outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. The adoption of the new requirements did not have a material impact on our consolidated financial statements or disclosures.

In August 2014, the FASB issued ASU No. 2014-15, “Presentation of Financial Statements – Going Concern”. This ASU codifies management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. The guidance is effective for annual periods ending after December 15, 2016, and for annual and interim periods thereafter, and early adoption is permitted. We do not expect that our adoption will have a material impact on our consolidated financial statements or disclosures.

In January 2015, the FASB issued ASU 2015-01, “Income Statement – Extraordinary and Unusual Items”. This ASU simplifies income statement classification by removing the concept of extraordinary items from U.S. GAAP. As a result, items that are both unusual and infrequent will no longer be separately reported net of tax after continuing operations. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015 and early adoption is permitted. The adoption of the new requirements did not have a material impact on our consolidated financial statements or disclosures.

In July 2015, the FASB issued ASU 2015-11, “Inventory – Simplifying the Measurement of Inventory”, which requires entities to measure most inventory “at the lower of cost and net realizable value (“NRV”), thereby simplifying the current guidance under which an entity must measure inventory at the lower of cost or market. The new guidance eliminates the need to determine replacement cost and evaluate whether it is above the ceiling (NRV) or below the floor (NRV less a normal profit margin). The guidance defines NRV as the “estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation”. The guidance is effective for



annual and interim periods beginning after December 15, 2016. Early application is permitted. We do not expect that the adoption of this guidance will have a significant impact on our consolidated financial statements.

In November 2015, the FASB issued ASU 2015-17, which requires all deferred tax assets and liabilities to be classified as non-current on the balance sheet instead of separating deferred taxes into current and non-current amounts. The guidance is effective for annual and interim periods beginning after December 15, 2016, and may be adopted on either a prospective or retrospective basis. We do not expect that our adoption will have a material impact on our consolidated financial statements or disclosures.

In February 2016, the FASB issued ASU 2016-02, "Leases", a comprehensive new standard that amends various aspects of existing accounting guidance for leases, including the recognition of a right of use asset and a lease liability for leases with a duration greater than one year. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. We have not completed our review of the new guidance; however, we anticipate that upon adoption of the standard, we will recognize additional assets and corresponding liabilities related to leases on our consolidated balance sheet.

## 2. NOTES PAYABLE AND LONG-TERM DEBT

On September 18, 2015, we executed a Promissory Note and Business Loan Agreement with BOKF, NA dba Bank of Texas ("BOKF"), which provides us with a line of credit facility of up to \$6,000,000. It has a two-year term and is secured by our inventory. The Business Loan Agreement contains covenants that we will maintain a funded debt to EBITDA ratio of no greater than 1.5 to 1, and that we will maintain a Fixed Charge Coverage Ratio greater than or equal to 1.2 to 1. Both ratios are calculated quarterly and are based on a trailing four quarter basis.

Also on September 18, 2015, we executed a Promissory Note with BOKF, which provides us with a line of credit facility of up to \$10,000,000 for the purpose of purchasing our common stock. Under the terms of the Promissory Note, we can borrow sums up to the lesser of \$10,000,000 or the purchase price of a maximum of 1.2 million shares of our common stock from the period September 18, 2015 and ending on the earlier of September 18, 2016 or the date on which the entire amount is drawn. During this time period, we will make interest only payments monthly. At the end of this time period, the principal balance will be rolled into a 4-year term note. This Promissory Note is secured by a Deed of Trust on the real estate located at 1900 SE Loop 820, Fort Worth, Texas. For the quarter ended March 31, 2016, we drew approximately \$2.9 million on this line of credit which was used to purchase approximately 404,000 shares of our common stock. At March 31, 2016, the unused portion of the line of credit was approximately \$3.4 million.

Amounts drawn under either Promissory Note accrue interest at the London interbank Eurodollar market rate for U.S. dollars (commonly known as "LIBOR") plus 1.85% (2.278% and 2.263% at March 31, 2016 and December 31, 2015, respectively).

On July 31, 2007, we entered into a Credit Agreement and Line of Credit Note with JPMorgan Chase Bank, N.A., pursuant to which the bank agreed to provide us with a credit facility of up to \$5,500,000 to facilitate our purchase of real estate consisting of a 191,000 square foot building situated on 30 acres of land located at 1900 SE Loop 820 in Fort Worth, Texas. Proceeds in the amount of \$4,050,000 were used to fund the purchase of the property that is our corporate headquarters. On April 30, 2008, the principal balance was rolled into a 10-year term note with an interest rate of 7.10% per annum. We paid this note in full in September 2015 and as a result of the early payoff, we incurred a prepayment penalty in the amount of \$200,000 which was included in interest expense.

On July 12, 2012, we executed a Line of Credit Note with JPMorgan Chase Bank, N.A., pursuant to which the bank agreed to provide us with a revolving credit facility of up to \$4 million, which was subsequently increased to \$6 million. The note expired on September 30, 2015. There was no balance owed on the line of credit at the expiration date.



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At March 31, 2016 and December 31, 2015, the amount outstanding under the above agreements consisted of the following:

|   | 2016        | 2015        |
|---|-------------|-------------|
| Business Loan Agreement with BOKF, NA – collateralized by real estate; payable as follows:  |             |             |
| Line of Credit Note dated September 18, 2015, in the maximum principal amount of \$10,000,000 with features as more fully described above – interest due monthly at LIBOR plus 1.85%; matures September 18, 2020          | \$6,581,224 | \$3,711,225 |
| Line of Credit Note dated September 18, 2015, in the maximum principal amount of \$6,000,000 with revolving features as more fully described above – interest due monthly at LIBOR plus 1.85%; matures September 18, 2017 | -           | -           |
|   | \$6,581,224 | \$3,711,225 |
| Less current maturities   | 822,653     | 231,952     |
|   | \$5,758,571 | \$3,479,273 |

### 3. CAPITAL LEASE OBLIGATIONS

We lease certain telecommunication equipment under a capital lease agreement. The asset subject to the agreement totaled \$227,783, of which \$22,152 is included in Property and Equipment at March 31, 2016 and December 31, 2015 and \$205,631 is included in Prepaid Equipment (not placed in service) as of March 31, 2016 and December 31, 2015. Accumulated depreciation on the assets placed in service was \$1,055 and \$264 at March 31, 2016 and December 31, 2015, respectively. Amortization of the capitalized cost is charged to depreciation expense.

At March 31, 2016 and December 31, 2015, the amounts outstanding under capital lease obligation consisted of the following:

|  | 2016      | 2015      |
|--|-----------|-----------|
| Capital Lease secured by certain telecommunication equipment – total annual principal payments of \$72,686, 1.8% interest, maturing January 2018 | \$149,251 | \$156,271 |
| Less amount representing interest  | 3,877     | 4,189     |
| Total obligation under capital lease   | 145,374   | 152,082   |
| Less - Current maturities  | 72,686    | 72,686    |
|  | \$72,688  | \$79,396  |

### 4. STOCK-BASED COMPENSATION

We have one stock option plan which permits annual stock option grants to non-employee directors with an exercise price equal to the fair market value of the shares at the date of grant. Options outstanding and exercisable were granted at a stock option price which was not less than the fair market value of our common stock on the date the option was granted and no option has a term in excess of ten years. Under this plan, no options were awarded to directors during the quarters ended March 31, 2016 and 2015 and therefore, no share based compensation expense was recorded for the quarters ended March 31, 2016 and 2015, respectively. During the three months ended March 31,

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2016 and 2015, the stock option activity under our stock option plans was as follows:

|                                 | Weighted<br>Average<br>Exercise<br>Price | # of shares | Weighted Average<br>Remaining<br>Contractual Term<br>(in years) | Aggregate<br>Intrinsic<br>Value |
|---------------------------------|--|-------------|---|---------------------------------|
| Outstanding, January 1,<br>2016 | \$5.17                                   | 68,400      |   |                                 |
| Granted                         | -  | -           |   |                                 |
| Cancelled                       | -  | -           |   |                                 |
| Exercised                       | -  | -           |   |                                 |
| Outstanding, March 31,<br>2016  | \$5.17                                   | 68,400      | 5.24  | \$83,933                        |
| Exercisable, March 31,<br>2016  | \$5.17                                   | 68,400      | 5.24  | \$83,933                        |
| Outstanding, January 1,<br>2015 | \$5.16                                   | 72,400      |   |                                 |
| Granted                         | -  | -           |   |                                 |
| Cancelled                       | -  | -           |   |                                 |
| Exercised                       | (4.96)                                   | (2,000)     |   |                                 |
| Outstanding, March 31,<br>2015  | \$5.17                                   | 70,400      | 6.07  | \$86,886                        |
| Exercisable, March 31,<br>2015  | \$5.17                                   | 70,400      | 6.07  | \$86,886                        |

Other information pertaining to option activity during the three-month periods ended March 31, 2016 and 2015 are as follows:

|   | March 31,<br>2016 | March 31, 2015 |
|---|-------------------|----------------|
| Weighted average grant-date fair value of stock options granted | N/A               | N/A            |
| Total fair value of stock options vested                        | N/A               | N/A            |
| Total intrinsic value of stock options exercised                | N/A               | \$2,953        |

As of March 31, 2016 and 2015, there was no unrecognized compensation cost related to non-vested stock options.

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We have a restricted stock plan that was adopted by our Board of Directors in January 2013 and approved by our stockholders in June 2013. The plan reserves up to 300,000 shares of our common stock for restricted stock awards to our executive officers, non-employee directors and other key employees. Awards granted under the plan may be stock awards or performance awards, and may be subject to a graded vesting schedule with a minimum vesting period of four years, unless otherwise determined by the committee that administers the plan.

In February 2015, our Chief Executive Officer, Chief Financial Officer and Senior Vice President were awarded restricted stock grants consisting of 9,343 shares each. In addition, four of our independent directors were awarded restricted stock grants consisting of 1,613 shares each. The grants will vest in equal annual amounts over a four-year period. The fair value of non-vested restricted common stock awards is the market value of our common stock on the date of grant. Compensation costs for these awards will be recognized on a straight-line basis over the four year vesting period.

In March 2016, our interim Chief Executive Officer and interim President were awarded restricted stock grants consisting of 11,765 shares each. In addition, our five independent directors were awarded restricted stock grants consisting of 2,031 shares each. The grants will vest in equal annual amounts over a four-year period. The fair value of non-vested restricted common stock awards is the market value of our common stock on the date of grant. Compensation costs for these awards will be recognized on a straight-line basis over the four year vesting period.

A summary of the activity for non-vested restricted common stock awards as of March 31, 2016 and 2015 is presented below:

|                                  | Shares   | Award<br>Fair Value |
|----------------------------------|----------|---------------------|
| Balance, January 1, 2016         | 60,433   | \$8.97              |
| Granted                          | 33,685   | \$7.14              |
| Forfeited                        | (8,187)  | 8.97                |
| Vested                           | (20,784) | 8.97                |
| Unvested Balance, March 31, 2016 | 65,147   | \$8.03              |
| Balance, January 1, 2015         | 34,601   | \$8.96              |
| Granted                          | 34,484   | \$8.99              |
| Forfeited                        | -        | -                   |
| Vested                           | (8,652)  | \$8.96              |
| Unvested Balance, March 31, 2015 | 60,433   | \$8.97              |

Total unrecognized compensation expense for the non-vested restricted stock awards as of March 31, 2016 and 2015 totals \$603,645 and \$523,154, respectively. As of March 31, 2016, compensation expense is expected to be recognized in equal annual amounts over a period of four years as follows:

|      | 2016 Award | 2015 Award | 2014 Award | Total     |
|------|------------|------------|------------|-----------|
| 2016 | \$45,095   | \$58,127   | \$58,130   | \$161,352 |
| 2017 | 60,128     | 77,503     | 77,506     | 215,137   |
| 2018 | 60,128     | 77,503     | 9,688      | 147,319   |
| 2019 | 60,128     | 9,688      | -          | 69,816    |
| 2020 | 10,021     | -          | -          | 10,021    |
|      | \$235,500  | \$222,821  | \$145,324  | \$603,645 |

## 5. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share (“EPS”) for the three months ended March 31, 2016 and 2015:

|  | 2016        | 2015        |
|--|-------------|-------------|
| Net income   | \$1,520,997 | \$1,444,407 |
| Numerator for basic and diluted earnings per share                   | \$1,520,997 | \$1,444,407 |
| Denominator for basic earnings per share – weighted-average shares   | 9,698,951   | 10,211,333  |
| Effect of dilutive securities:                                       |             |             |
| Stock options  | 19,461      | 29,763      |
| Restricted stock   | 41          | -           |
| Dilutive potential common shares                                     | 19,502      | 29,763      |
| Denominator for diluted earnings per share – weighted-average shares | 9,718,453   | 10,241,096  |
| Basic earnings per share   | \$0.16      | \$0.14      |
| Diluted earnings per share   | \$0.16      | \$0.14      |

The net effect of assuming the exercise of all potentially dilutive common share equivalents, including stock options to purchase common stock at exercise prices less than the average market prices and restricted stock awards of an aggregate of 149,922 and 130,833 shares of common stock have been included in the computations of diluted EPS for the quarters ended March 31, 2016 and 2015, respectively.

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## 6. COMMITMENTS AND CONTINGENCIES

Legal Proceedings. We are periodically involved in litigation that arises in the ordinary course of business and operations. There are no such matters pending that we expect to have a material impact on our financial position and operating results. Legal costs associated with the resolution of claims, lawsuits and other contingencies are expensed as incurred.

## 7. SEGMENT INFORMATION

We identify our segments based on the activities of three distinct operations:

- a. Wholesale Leathercraft, which consists of a chain of wholesale stores operating under the name, The Leather Factory, located in North America;
- b. Retail Leathercraft, which consists of a chain of retail stores operating under the name, Tandy Leather Company, located in North America; and
- c. International Leathercraft, which sells to both wholesale and retail customers. We have four stores operating in this segment: one in Northampton, United Kingdom; one in Manchester, United Kingdom (which opened in October 2015); one in Sydney, Australia; and one in Jerez, Spain. These stores carry the same products as our North American stores.

Our reportable operating segments have been determined as separately identifiable business units, and we measure segment earnings as operating earnings, defined as income before interest and income taxes.

|                                      | Wholesale<br>Leathercraft | Retail<br>Leathercraft | Int'l<br>Leathercraft | Total        |
|--------------------------------------|---------------------------|------------------------|-----------------------|--------------|
| For the quarter ended March 31, 2016 |                           |                        |                       |              |
| Net sales                            | \$6,496,908               | \$13,242,583           | \$932,736             | \$20,672,227 |
| Gross profit                         | 4,388,629                 | 7,696,180              | 567,937               | 12,652,746   |
| Income from operations               | 1,126,259                 | 1,214,950              | 21,581                | 2,362,790    |
| Interest expense                     | 23,429                    | -                      | -                     | 23,429       |
| Other, net                           | (5,746)                   | -                      | 5,785                 | 39           |
| Income before income taxes           | 1,108,576                 | 1,214,950              | 15,796                | 2,339,322    |
| Depreciation and amortization        | 241,899                   | 151,693                | 20,636                | 414,228      |
| Fixed asset additions                | 371,299                   | 231,565                | 4,068                 | 606,932      |
| Total assets                         | \$41,849,437              | \$18,296,478           | \$5,113,930           | \$65,259,845 |
| For the quarter ended March 31, 2015 |                           |                        |                       |              |
| Net sales                            | \$6,725,304               | \$13,109,413           | \$954,047             | \$20,788,764 |
| Gross profit                         | 4,169,635                 | 7,845,766              | 567,527               | 12,582,928   |
| Income from operations               | 951,855                   | 1,403,452              | 33,574                | 2,388,881    |
| Interest expense                     | 44,163                    | -                      | -                     | 44,163       |
| Other, net                           | (11,393)                  | -                      | (8,480)               | (19,873)     |
| Income before income taxes           | 919,085                   | 1,403,452              | 42,054                | 2,364,591    |
| Depreciation and amortization        | 239,718                   | 132,862                | 11,356                | 383,936      |
| Fixed asset additions                | 419,906                   | 257,538                | -                     | 677,444      |
| Total assets                         | \$39,891,481              | \$16,388,517           | \$3,357,336           | \$59,637,334 |

Net sales for geographic areas were as follows for the three months ended March 31:

|                     | 2016         | 2015         |
|---------------------|--------------|--------------|
| United States       | \$17,727,629 | \$17,748,632 |
| Canada              | 1,741,756    | 1,899,118    |
| All other countries | 1,202,842    | 1,141,014    |
|                     | \$20,672,227 | \$20,788,764 |

Geographic sales information is based on the location of the customer. No single foreign country, except for Canada, accounted for any material amount of our consolidated net sales for the three-month periods ended March 31, 2016 and 2015. We do not have any significant long-lived assets outside of the United States.



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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Our Business

We are the world's largest specialty retailer and wholesale distributor of leather and leathercraft related items. We market our products to our growing list of customers through company-owned retail and wholesale stores. We are a Delaware corporation, and our common stock trades on the NASDAQ Global Market under the symbol "TLF." We operate our business in three segments: Wholesale Leathercraft, which operates wholesale stores in North America under the trade name, The Leather Factory, Retail Leathercraft, which operates retail stores in North America under the trade name, Tandy Leather Company, and International Leathercraft, which operates combination retail/wholesale stores outside of North America under the trade name, Tandy Leather Factory. See Note 7 to the Consolidated Financial Statements for additional information concerning our segments, as well as our foreign operations.

Our Wholesale Leathercraft segment operates 28 company-owned wholesale stores in 18 states and three Canadian provinces. These stores are engaged in the wholesale distribution of leather and related items, including leatherworking tools, buckles and belt adornments, leather dyes and finishes, saddle and tack hardware, and do-it-yourself kits, to retailers, manufacturers, and end users.

Our Retail Leathercraft segment operates company-owned Tandy Leather Company retail stores in 38 states and six Canadian provinces. Tandy Leather Company, one of the best-known suppliers of leather and related supplies used in the leathercraft industry, has been a primary leathercraft resource for decades. Tandy Leather Company's products include quality tools, leather, accessories, kits and teaching materials. In 2002, we began expanding our industry presence by opening retail stores. As of May 1, 2016, we were operating 82 Tandy Leather Company retail stores located throughout North America.

Our International Leathercraft segment operates 4 company-owned stores, all located outside of North America. These stores operate as combination retail / wholesale stores and consist of one store in Northampton, United Kingdom; one store in Manchester, United Kingdom; one store in Sydney, Australia, and one store in Jerez, Spain. We expect to continue opening international stores in the future, but do not intend to open any new stores in 2016.

Critical Accounting Policies

A description of our critical accounting policies appears in Item 7 "Management's Discussions and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015.

Forward-Looking Statements

Certain statements contained in this report and other materials we file with the Securities and Exchange Commission, as well as information included in oral statements or other written statements made or to be made by us, other than statements of historical fact, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements generally are accompanied by words such as "may," "will," "could," "should," "anticipate," "believe," "budgeted," "intend," "plan," "project," "potential," "estimate," "continue," or "future" variations thereof or other similar statements. There are certain important risks that could cause results to differ materially from those anticipated by some of the forward-looking statements. Some, but not all, of the important risks, including, without limitation, those described below, could cause actual results to differ materially from those suggested by the forward-looking statements. Please

refer also to our Annual Report on Form 10-K for fiscal year ended December 31, 2015 for additional information concerning these and other uncertainties that could negatively impact the Company. Potential factors, which could cause our actual results of operations to differ materially from those in the forward-looking statements include, among others:

- Ø General economic conditions in the United States and abroad;
  - Ø Increased pressure on margins;
- Ø Increases in the cost of the products we sell or a reduction in availability of those products;
  - Ø Challenges in implementing our planned international expansion;
    - Ø Failure to open additional stores in North America;
  - Ø Failure to hire and train qualified personnel to operate new and existing stores;
  - Ø Failure to protect our trademarks and other proprietary intellectual property rights;
- Ø Negative impact of foreign currency fluctuations on our financial condition and results of operations;
  - Ø Damage to our brand image.

We assume no obligation to update or otherwise revise our forward-looking statements even if experience or future changes make it clear that any projected results, express or implied, will not be realized.

#### Results of Operations

The following tables present selected financial data of each of our three segments for the quarters ended March 31, 2016 and 2015.

|                            | Quarter Ended March 31, 2016 |                        | Quarter Ended March 31, 2015 |                        |
|----------------------------|------------------------------|------------------------|------------------------------|------------------------|
|                            | Sales                        | Income from Operations | Sales                        | Income from Operations |
| Wholesale Leathercraft     | \$6,496,908                  | \$1,126,259            | \$6,725,304                  | \$951,855              |
| Retail Leathercraft        | 13,242,583                   | 1,214,950              | 13,109,413                   | 1,403,452              |
| International Leathercraft | 932,736                      | 21,581                 | 954,047                      | 33,574                 |
| Total Operations           | \$20,672,227                 | \$2,362,790            | \$20,788,764                 | \$2,388,881            |

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Consolidated net sales for the quarter ended March 31, 2016 decreased \$117,000, or 0.6%, compared to the same period in 2015. Retail Leathercraft reported a sales gain of 1%, while Wholesale Leathercraft and International Leathercraft reported sales declines of 3.4% and 2.2%, respectively. Income from operations on a consolidated basis for the quarter ended March 31, 2016 decreased 1%, or \$26,000, from the first quarter of 2015 primarily due to an increase in operating expenses, offset by an improvement in gross profit.

The following table shows in comparative form our consolidated net income for the first quarters of 2016 and 2015:

|            | 2016        | 2015        | % change |
|------------|-------------|-------------|----------|
| Net income | \$1,520,997 | \$1,444,407 | 5.3%     |

All segments were profitable in the first quarter of 2016. Additional information appears below for each segment.

## Wholesale Leathercraft

Our Wholesale Leathercraft operation consists of 28 wholesale stores (there were no wholesale stores opened or closed in either the first quarter of 2016 or 2015). The following table presents the combined sales mix by customer categories for the quarters ended March 31:

| Customer Group  | Quarter ended |          |
|---|---------------|----------|
|   | 03/31/16      | 03/31/15 |
| RETAIL (end users, consumers, individuals)  | 48%           | 49%      |
| INSTITUTION (prisons, prisoners, hospitals, schools, youth organizations, etc.)     | 2%            | 3%       |
| WHOLESALE (resellers & distributors, saddle & tack shops, authorized dealers, etc.) | 43%           | 41%      |
| MANUFACTURERS   | 6%            | 6%       |
| NATIONAL ACCOUNTS   | 1%            | 1%       |
|   | 100%          | 100%     |

Net sales decreased 3.4%, or \$228,000, for the first quarter of 2016 compared to the first quarter of 2015. Sales to our wholesale and manufacturing customers increased in the first quarter of 2016 compared to the first quarter of 2015, while sales to our other customer groups declined slightly. Income from operations for Wholesale Leathercraft during the current quarter increased by 18.3% or \$174,000 from the comparative 2015 quarter.

An increase in gross profit of \$219,000 offset by an increase in operating expenses of \$45,000 contributed to the improvement in income from operations. Gross profit as a percentage of sales increased from 62.0% in the first quarter of 2015 to 67.6% in the first quarter of 2016, due to an increase in sales of higher margin products compared to last year's first quarter. Operating expenses increased 1.4%, or \$45,000, compared to last year's comparable period. The most significant expense increase occurred in legal and professional fees, offset somewhat by a reduction in travel and moving expenses.

## Retail Leathercraft

Our Retail Leathercraft operation consisted of 82 stores at both March 31, 2016 and March 31, 2015. Net sales increased 1.0% for the first quarter of 2016 over the same quarter last year. In the first quarter of 2016, one new store was opened in Nyack, NY and one store was closed in Tucson, AZ. A store is categorized as "new" until it is operating for the full comparable period in the prior year.

| # | Qtr Ended | # | Qtr Ended | \$ | % |
|---|-----------|---|-----------|----|---|
|---|-----------|---|-----------|----|---|

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|                    | Stores | 03/31/16     | Stores | 03/31/15     | Change    | Change |
|--------------------|--------|--------------|--------|--------------|-----------|--------|
| Same store sales   | 82     | \$13,059,658 | 82     | \$13,019,613 | \$40,045  | 0.3%   |
| New store sales    | 1      | 79,654       | -      | -            | 79,654    | N/A    |
| Closed store sales | 1      | 103,271      | -      | 89,800       | 13,471    | 15.0%  |
| Total sales        |        | \$13,242,583 |        | \$13,109,413 | \$133,170 | 1.0%   |

The following table presents sales mix by customer categories for the quarters ended March 31, 2016 and 2015 for our Retail Leathercraft operation:

| Customer Group  | Quarter ended |          |
|---|---------------|----------|
|   | 03/31/16      | 03/31/15 |
| RETAIL (end users, consumers, individuals)  | 60%           | 61%      |
| INSTITUTION (prisons, prisoners, hospitals, schools, youth organizations, etc.)     | 2%            | 3%       |
| WHOLESALE (resellers & distributors, saddle & tack shops, authorized dealers, etc.) | 35%           | 34%      |
| MANUFACTURERS   | 3%            | 2%       |
|   | 100%          | 100%     |

Sales to our wholesale and manufacturing customers increased in the first quarter of 2016 compared to the first quarter of 2015, while sales to our other customer groups declined slightly.

Income from operations decreased \$189,000, or 13.4%, from the comparative 2015 quarter due to a decrease in gross profit and an increase in operating expenses. Our gross profit decreased by \$150,000 from the prior period and as a percentage of sales, gross profit margin declined from 59.9% in the first quarter of 2015 to 58.1% in the first quarter of 2016. The increase in sales was primarily to wholesale customers, causing the decrease in our gross profit margin percentage. Operating expenses as a percentage of sales decreased from 49.1% in the first quarter of 2015 to 48.9% in the first quarter of 2016. The increase in operating expenses of \$39,000 compared to the first quarter of 2015 was caused primarily by an increase in rent expense, partially offset by a decrease in freight out.

#### International Leathercraft

International Leathercraft consists of all stores located outside of North America. As of March 31, 2016, the segment contained four stores, two of which are located in United Kingdom (one of which opened in October 2015) and one each in Australia and Spain. This segment's sales totaled \$933,000 for the first quarter of 2016, compared to \$954,000 in the first quarter of 2015, a decrease of 2.2%. Gross profit margin improved from 59.5% in 2015 compared to 60.9% in 2016, while operating expenses increased by \$12,000. Operating expenses totaled \$546,000 in the first quarter of 2016, up from \$534,000 in the first quarter of 2015. Advertising and marketing expenses are this segment's largest expense, followed by employee compensation, rent, travel, and shipping costs to customers.

#### Other Expenses

We paid \$23,000 in interest on our bank debt in the first quarter of 2016, compared to \$44,000 in the first quarter of 2015. We recorded expense of \$8,000 for currency fluctuations in the first quarter of 2016. Comparatively, in the first quarter of 2015, we recorded income of \$10,000 for currency fluctuations.

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Capital Resources, Liquidity and Financial Condition

On our consolidated balance sheet, total assets increased from \$64.6 million at year-end 2015 to \$65.3 million at March 31, 2016. Total stockholders' equity decreased from \$51.0 million at December 31, 2015 to \$50.3 million at March 31, 2016, the decrease being attributable \$2.9 million of treasury stock purchases offset by our net income earned in the first quarter of 2016. Our current ratio increased from 5.7 at December 31, 2015 to 6.5 at March 31, 2016 due primarily to the reduction in accrued liabilities for bonuses paid in the first quarter of 2016.

As of March 31, 2016, our investment in inventory increased by \$48,000 from year-end 2015. Inventory turnover reached an annualized rate of 2.5 times during the first quarter of 2016, decreasing from 2.6 times for the first quarter of 2015. Inventory turnover was 2.5 times for all of 2015. We compute our inventory turns as sales divided by average inventory.

Trade accounts receivable was approximately \$683,000 at March 31, 2016, up \$130,000 from \$553,000 at year-end 2015. The average days to collect accounts decreased to 34 days for the first quarter of 2016, a slight improvement from the average days to collect accounts in the first quarter of 2015 of 35 days. We are continually monitoring our customer accounts very closely in order to minimize the risk of uncollectible accounts.

Accounts payable decreased approximately \$63,000 to \$1.9 million at March 31, 2016 compared to \$2.0 million at year-end 2015 due to timing of payments. Accrued expenses decreased from \$6.0 million at December 31, 2015 to \$4.6 million at March 31, 2016. The payment of the 2015 manager bonuses during the first quarter of 2016 primarily accounted for the reduction.

During the first quarter of 2016, cash flow provided by operating activities was \$1.1 million, composed of net income of \$1.5 million, plus \$414,000 of depreciation and amortization, plus \$614,000 of foreign currency translation, offset by the decrease in accrued expenses and other liabilities of \$1.5 million.

By comparison, during the first quarter of 2015, cash flow provided by operating activities was \$3.5 million. The decrease in inventory of \$2.5 million and net income of \$1.4 million accounted for the operating cash provided during the first quarter of 2015.

Cash flow used in investing activities totaled approximately \$584,000 and \$675,000 in the first quarters of 2016 and 2015, respectively, consisting primarily of the purchase of fixtures for store moves and remodels and computer equipment.

Cash flow used in financing activities totaled \$7,450 in the first quarter of 2016, compared to \$3.5 million in the first quarter of 2015. In 2016, we purchased \$2.9 million of treasury stock, funded primarily through drawdowns on our line of credit with BOKF. We also made a scheduled payment on our capital lease obligation for \$6,710. In 2015, cash used consisted primarily of debt repayments.

We expect to fund our operating and liquidity needs as well as our store growth from a combination of current cash balances and internally generated funds.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

For disclosures about market risk affecting us, see Item 7A "Quantitative and Qualitative Disclosures About Market Risk" in our Annual Report on Form 10-K for fiscal year ended December 31, 2015. We believe that our exposure to market risks has not changed significantly since December 31, 2015. We expect that our exposure to foreign currency exchange risk will increase as our international presence increases.

## Item 4. Controls and Procedures.

## Evaluation of Disclosure Controls and Procedures

Our management team, under the supervision and with the participation of our principal executive officer and our principal financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, as of the last day of the fiscal period covered by this report, March 31, 2016. The term disclosure controls and procedures means our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934, as amended, is accumulated and communicated to management, including our principal executive and principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based on this evaluation, our principal executive officer and our principal financial officer concluded that, as of March 31, 2016, our disclosure controls and procedures were effective at a reasonable assurance level.

## Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting during the fiscal quarter ended March 31, 2016 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

## Item 1. Legal Proceedings.

The information contained in Note 6 to the consolidated financial statements included in Item 1 of this Report is hereby incorporated into this Item 1 by reference.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

## Purchases of Equity Securities by the Issuer and Affiliated Purchasers

The following table provides information about purchases we have made of our common stock during the quarter ended March 31, 2016:

| ISSUER PURCHASES OF EQUITY SECURITIES |                                      |                                  |  |  |
|---------------------------------------|--------------------------------------|----------------------------------|--|--|
| Period                                | (a) Total Number of Shares Purchased | (b) Average Price Paid per Share | (c) Total Number of  | (d) Maximum Number of  |
|                                       |                                      |                                  | Shares Purchased as Part of Publicly Announced Plans or Programs | Shares that May Yet Be Purchased Under the Plans or Programs |
| January 1 – January 31                | -                                    | -                                | -  | 671,275  |
| February 1 – February 29              | -                                    | -                                | -  | 671,275  |
| March 1 – March 31                    | 404,423 (1)                          | \$7.10                           | 404,423  | 266,852  |
| Total                                 | 404,423                              | \$7.10                           | 404,423  | 266,852  |

- (1) Represents shares purchased through a stock repurchase program permitting us to repurchase up to 1.2 million shares of our common stock at prevailing market prices. We announced the program on August 10, 2015. Purchases under the program commenced on August 24, 2015 and will terminate on August 9, 2016.

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## Item 6. Exhibits.

| Exhibit Number | Description  |
|----------------|--|
| 3.1            | Certificate of Incorporation of The Leather Factory, Inc., and Certificate of Amendment to Certificate of Incorporation of The Leather Factory, Inc. filed as Exhibit 3.1 to Tandy Leather Factory, Inc.'s Form 10-Q filed with the Securities and Exchange Commission on August 12, 2005 and incorporated by reference herein.  |
| 3.2            | Bylaws of The Leather Factory, Inc. (n/k/a Tandy Leather Factory, Inc.), filed as Exhibit 3.5 to the Current Report on Form 8-K (Commission File No. 001-12368) filed by Tandy Leather Factory, Inc (f/k/a The Leather Factory, Inc.) with the Securities and Exchange Commission on July 14, 2004 and incorporated by reference herein.   |
| 3.3            | Certificate of Designations of Series A Junior Participating Preferred Stock of Tandy Leather Factory, Inc. filed as Exhibit 3.1 to Tandy Leather Factory's Inc.'s Current Report on Form 8-K filed with the Securities and Exchange Commission on June 10, 2013 and incorporated by reference herein.   |
| 4.1            | Rights Agreement dated as of June 6, 2013 between Tandy Leather Factory, Inc. and Broadridge Corporate Issuer Solutions, Inc., as Rights Agent (including the Certificate of Designations of Series A Junior Preferred Stock attached thereto as Exhibit A, the form of Right Certificate attached thereto as Exhibit B and the Summary of Rights attached thereto as Exhibit C), filed as Exhibit 4.1 to Tandy Leather Factory Inc.'s Current Report on Form 8-K filed with the Securities and Exchange Commission on June 10, 2013 and incorporated by reference herein. |
| 10.1           | 2007 Director Non-Qualified Stock Option Plan, filed as Exhibit A to Tandy Leather Factory, Inc.'s Definitive Proxy Statement on Schedule 14A filed with the Securities and Exchange Commission on April 18, 2007 and incorporated by reference herein.  |
| 10.2           | First Amendment to 2007 Director Non-Qualified Stock Option Plan dated May 3, 2010, filed as Exhibit 10.2 to Tandy Leather Factory Inc.'s Current Report on Form 8-K filed with the Securities and Exchange Commission on May 4, 2010 and incorporated by reference herein.  |
| 10.3           | Second Amendment to 2007 Director Non-Qualified Stock Option Plan dated October 7, 2010, filed as Exhibit 10.3 to Tandy Leather Factory Inc.'s Current Report on Form 8-K filed with the Securities and Exchange Commission on October 12, 2010 and incorporated by reference herein.  |
| 10.4           | Third Amendment to 2007 Director Non-Qualified Stock Option Plan dated February 11, 2014, filed as Exhibit 10.5 to Tandy Leather Factory Inc.'s Current Report on Form 8-K filed with the Securities and Exchange Commission on February 14, 2014 and incorporated by reference herein.  |
| 10.5           | Business Loan Agreement, dated September 18, 2015, by and between Tandy Leather Factory, Inc. and BOKF, NA dba Bank of Texas, filed as Exhibit 10.2 to Tandy Leather Factory's Current Report on Form 8-K filed with the Securities and Exchange Commission on September 24, 2015 and incorporated by reference herein.  |



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|----------|---|
| 10.6     | \$6,000,000 Promissory Note, dated September 18, 2015, by and between Tandy Leather Factory, Inc. and BOKF, NA dba Bank of Texas, filed as Exhibit 10.1 to Tandy Leather Factory's Current Report on Form 8-K filed with the Securities and Exchange Commission on September 24, 2015 and incorporated by reference herein.                     |
| 10.7     | \$10,000,000 Promissory Note, dated September 18, 2015, by and between Tandy Leather Factory, Inc. and BOKF, NA dba Bank of Texas, filed as Exhibit 10.3 to Tandy Leather Factory's Current Report on Form 8-K filed with the Securities and Exchange Commission on September 24, 2015 and incorporated by reference herein.                    |
| 10.8     | Deed of Trust, dated as of September 18, 2015, by and among Tandy Leather Factory, Inc., Jeffrey L. Seasor and BOKF, NA dba Bank of Texas, filed as Exhibit 10.1 to Tandy Leather Factory's Current Report on Form 8-K filed with the Securities and Exchange Commission on September 24, 2015 and incorporated by reference herein.            |
| 10.9     | Form of Change of Control Agreement between the Company and each of Jon Thompson, Shannon Greene and Mark Angus, each effective as of December 3, 2012, filed as Exhibit 10.1 to Tandy Leather Factory's Current Report on Form 8-K filed with the Securities and Exchange Commission on December 6, 2012 and incorporated by reference herein. |
| 10.10    | Tandy Leather Factory, Inc. 2013 Restricted Stock Plan, filed as Exhibit 10.1 to Tandy Leather Factory's Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 14, 2013 and incorporated by reference herein.   |
| 10.11    | Form of Non-Employee Director Restricted Stock Agreement under Tandy Leather Factory, Inc.'s 2013 Restricted Stock Plan, filed as Exhibit 10.1 to Tandy Leather Factory, Inc.'s Current Report on Form 8-K filed with the Securities and Exchange Commission on February 14, 2014 and incorporated by reference herein.                         |
| 10.12    | Form of Employee Restricted Stock Agreement under Tandy Leather Factory, Inc.'s 2013 Restricted Stock Plan, filed as Exhibit 10.6 to Tandy Leather Factory, Inc.'s Current Report on Form 8-K, filed with the Securities and Exchange Commission on February 14, 2014 and incorporated by reference herein.                                     |
| *31.1    | 13a-14(a) or 15d-14(a) Certification by Shannon L. Greene, Interim Chief Executive Officer.   |
| *31.2    | 13a-14(a) or 15d-14(a) Certification by Shannon L. Greene, Chief Financial Officer and Treasurer.   |
| *32.1    | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted 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 Document.   |
| *101.DEF | XBRL Taxonomy Extension Definition Document.  |
| *101.LAB | XBRL Taxonomy Extension Labels Document.  |

\*101.PRE XBRL Taxonomy Extension Presentation Document.

\*Filed herewith.

#### SIGNATURES

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

TANDY LEATHER FACTORY, INC.  
(Registrant)

Date: May 16, 2016

By: /s/ Shannon L. Greene  
Shannon L. Greene  
Interim Chief Executive Officer and  
Chief Financial Officer and Treasurer (Chief Accounting  
Officer)