

ETHAN ALLEN INTERIORS INC  
Form 10-K  
August 02, 2018

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

(Mark One)

**[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended June 30, 2018

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 1-11692

Ethan Allen Interiors Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

06-1275288

(I.R.S. Employer Identification No.)

25 Lake Avenue Extension, Danbury, CT 06811

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code (203) 743-8000

Securities registered pursuant to Section 12(b) of the Act:

| Title of Each Class           | Name of Each Exchange On Which Registered |
|-------------------------------|-------------------------------------------|
| Common Stock, \$.01 par value | New York Stock Exchange, Inc.             |

Securities registered pursuant to Section 12(g) of the Act:

None

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(Title of Class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ☒ Yes ☐ No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ☐ Yes ☒ No

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 such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒ X

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

|                         |                                     |                                            |                                                    |
|-------------------------|-------------------------------------|--------------------------------------------|----------------------------------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer                          | <input type="checkbox"/>                           |
| Non-accelerated filer   | <input type="checkbox"/>            | Do not check if smaller reporting company) | Smaller reporting company <input type="checkbox"/> |
| Emerging growth company | <input type="checkbox"/>            |                                            |                                                    |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to section 13(a) of the Exchange Act. ☐

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

The aggregate market value of the voting and non-voting stock held by non-affiliates of the registrant on December 31, 2017, the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$716,611,000. As of July 27, 2018, there were 26,529,294 shares of the registrant's common stock, par value \$.01 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE: Certain designated information contained in the registrant's definitive Proxy Statement for the 2018 Annual Meeting of stockholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A of the Securities Exchange Act of 1934, is incorporated by reference into Part III hereof to the extent described herein.

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**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

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## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **PART I**

#### **Item 1. Business**

##### **Overview**

Founded in 1932 and incorporated in Delaware in 1989, Ethan Allen Interiors Inc., through its wholly-owned subsidiary, Ethan Allen Global, Inc., and Ethan Allen Global, Inc.'s subsidiaries (collectively, "We," "Us," "Our," "Ethan Allen" or the "Company"), is a leading interior design company and manufacturer and retailer of quality home furnishings. Today we are a leading international home fashion brand doing business in North America, Asia, the Middle East and Europe. We are vertically integrated from design through delivery, affording our clientele a value proposition of style, quality and price. We offer complimentary interior design service to our clients and sell a full range of furniture products and decorative accents through ethanallen.com and a retail network of approximately 300 design centers in the United States and abroad. The design centers represent a mix of independent licensees and our own Company operated retail segment. We own and operate nine manufacturing facilities including six manufacturing plants and one sawmill in the United States and one manufacturing plant in Mexico and one in Honduras. Approximately 75% of the products sold by the Company are manufactured in our North American plants.

##### **Available Information**

Our website is [www.ethanallen.com](http://www.ethanallen.com). Information contained on our website is not part of this Annual Report on Form 10-K. Information that we furnish or file with the Securities and Exchange Commission (the "SEC"), including our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to, or exhibits included in, these reports are available for download, free of charge, on our website soon after such reports are filed with or furnished to the SEC. Our SEC filings, including exhibits filed therewith, are also available on the SEC's website at [www.sec.gov](http://www.sec.gov). You may obtain and copy any document we furnish or file with the SEC at the SEC's public reference room at 100 F Street, NE, Room 1580, Washington, D.C. 20549. You may obtain information on the operation of the SEC's public reference facilities by calling the SEC at 1-800-SEC-0330. You may request copies of these documents, upon payment of a duplicating fee, by writing to the SEC at its principal office at 100 F Street, NE, Room 1580, Washington, D.C. 20549.

## **Operating Segments**

Our two operating segments, the wholesale segment and the retail segment, represent strategic business areas of our vertically integrated enterprise that operate separately and provide their own distinctive services. This vertical structure enables us to offer our complete line of home furnishings and accents while controlling quality and cost more effectively. We evaluate performance of the respective segments based upon revenues and operating income. Inter-segment transactions result, primarily, from the wholesale sale of inventory to the retail segment, including the related profit margin. For certain financial information regarding our operating segments, see Note 15 to the Consolidated Financial Statements included under Item 8 of this Annual Report and incorporated herein by reference.

As of June 30, 2018, the Company operated 148 design centers (our retail segment) and our independent retailers operated 148. Our wholesale segment net sales include sales to our retail segment, which are eliminated in consolidation, sales to our independent retailers and contract sales to unaffiliated third parties. Our retail segment net sales accounted for 77% of our consolidated net sales in fiscal 2018. Our wholesale segment net sales accounted for 23%, including 15.5% of our consolidated net sales in fiscal 2018 to ten of our largest customers, which includes the General Services Administration (“GSA”) government contract business, and licensees operating 105 design centers.

### ***Wholesale Segment Overview:***

The wholesale segment, principally involved in the development of the Ethan Allen brand, encompasses all aspects of design, manufacture, sourcing, marketing, sale, and distribution of our broad range of home furnishings and accents. Wholesale revenue is generated upon the sale and shipment of our products to our retail network of independently operated design centers, Company operated design centers and other contract customers.

Within the wholesale segment, we maintain revenue information according to each respective product line (i.e. case goods, upholstery, and home accents and other). Case goods include items such as beds, dressers, armoires, tables, chairs, buffets, entertainment units, home office furniture, and wooden accents. Upholstery items include sleepers, recliners and other motion furniture, chairs, ottomans, custom pillows, sofas, loveseats, cut fabrics and leather. Skilled artisans cut, sew and upholster custom-designed upholstery items which are available in a variety of frame, fabric and trim options. Home accent and other items include window treatments and drapery hardware, wall decor, florals, lighting, clocks, mattresses, bedspreads, throws, pillows, decorative accents, area rugs, wall coverings and home and garden furnishings.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

Wholesale net sales for each of the last three fiscal years, allocated by product line, were as follows:

|                        | Fiscal Year Ended<br>June 30, |   |      |   |      |   |
|------------------------|-------------------------------|---|------|---|------|---|
|                        | 2018                          |   | 2017 |   | 2016 |   |
| Case Goods             | 32                            | % | 33   | % | 32   | % |
| Upholstered Products   | 51                            | % | 51   | % | 51   | % |
| Home Accents and Other | 17                            | % | 16   | % | 17   | % |
|                        | 100                           | % | 100  | % | 100  | % |

As of June 30, 2018, our wholesale backlog was \$56.5 million (as compared to \$47.4 million as of June 30, 2017) which is anticipated to be serviced in the first quarter of fiscal 2019. This backlog fluctuates based on the timing of net orders booked, manufacturing schedules and efficiency, the timing of sourced product receipts, the timing and volume of wholesale shipments, and the timing of various promotional events. Because orders may be rescheduled and/or canceled and the sourcing timing may change, the measure of backlog at a point in time is not necessarily indicative of future sales performance.

Our independent retailers are required to enter into license agreements with us, which (i) authorize the use of certain Ethan Allen trademarks and (ii) require adherence to certain standards of operation, including a requirement to fulfill related warranty service agreements. We are not subject to any territorial or exclusive retailer agreements in North America.

Wholesale profitability includes (i) the wholesale gross margin, which represents the difference between the wholesale net sales price and the cost associated with manufacturing and/or sourcing the related product, and (ii) other operating costs associated with wholesale segment activities.

### ***Retail Segment Overview:***

The retail segment sells home furnishings and accents to consumers through a network of Company operated design centers. Retail revenue is generated upon the retail sale and delivery of our products to our retail customers through our network of service centers. Retail profitability reflects (i) the retail gross margin, which represents the difference between the retail net sales price and the cost of goods, purchased primarily from the wholesale segment, and (ii) other operating costs associated with retail segment activities.



We measure the performance of our design centers based on net sales and written orders booked on a comparable period basis. Comparable design centers are those which have been operating for at least 15 months, including relocated design centers provided the original and relocated design center location had been operating for at least 15 months on a combined basis. During the first three months of operations of newly opened design centers, written orders are booked but minimal net sales are achieved through the delivery of products. Design centers we acquire from independent retailers are included in comparable design center sales in their 13th full month of Ethan Allen-owned operations. The frequency of our promotional events as well as the timing of the end of those events can also affect the comparability of orders booked during a given period. During fiscal 2018, the Company added five new design centers in the United States, including two acquired from independent retailers and one relocation, and closed five locations, including one relocation. The geographic distribution of retail design center locations is included under Item 2 of Part I of this Annual Report.

Retail net sales for each of the last three fiscal years, allocated by product line, were as follows:

|                        | Fiscal Year Ended<br>June 30, |   |      |   |      |   |
|------------------------|-------------------------------|---|------|---|------|---|
|                        | 2018                          |   | 2017 |   | 2016 |   |
| Case Goods             | 30                            | % | 30   | % | 31   | % |
| Upholstered Products   | 48                            | % | 48   | % | 47   | % |
| Home Accents and Other | 22                            | % | 22   | % | 22   | % |
|                        | 100                           | % | 100  | % | 100  | % |

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **Products**

Our strategy has been to position Ethan Allen as a preferred brand offering complimentary design service together with products of superior style, quality and value to provide consumers with a comprehensive, one-stop shopping solution for their home furnishing and interior design needs. In carrying out our strategy, we continue to expand our reach to a broader consumer base through a diverse selection of attractively priced products, designed to complement one another, reflecting current fashion trends in home decorating. We continuously monitor changes in home fashion trends through attendance at international industry events and fashion shows, internal market research, and regular communication with our retailers and design center design consultants who provide valuable input on consumer trends. We believe that the observations and input gathered enable us to incorporate appropriate style details into our products to react quickly to changing consumer tastes.

75% of our furniture is built by artisans, one piece at a time, in our North American workshops. Most upholstery frames are hand-assembled and stitching is guided by hand. We select international partners who are as committed to quality and social responsibility as we are. All case goods frames are made with premium lumber and veneers. We use best-in-class construction techniques, including mortise and tenon joinery and four-corner glued dovetail joinery on drawers. We combine technology with personal service and maintain an up-to-date broad range of styles and custom options in keeping with today's home decorating trends. These factors continue to define Ethan Allen, positioning us as a fashion leader in the home furnishing industry.

The interior of our design centers, which were substantially refreshed during the past three fiscal years, are organized to facilitate display of our product offerings, both in room settings that project the category lifestyle and by product grouping to facilitate comparisons of the styles and tastes of our clients. To further enhance the experience, technology is used to expand the range of products viewed by including content from our website in applications used on large touch-screen flat panel displays.

### **Product Development and Sourcing Activities**

Using a combination of on staff and outsourced product designers, we design the majority of the products we sell. All our products are branded Ethan Allen. This important facet of our vertically integrated business enables us to control the design specifications and establish consistent levels of quality across the products in our own North American plants. In addition to our seven U.S. manufacturing facilities, we have an upholstery manufacturing facility in Mexico and a case goods manufacturing facility in Honduras. Approximately 75% of the products we sell are manufactured or assembled in these North American facilities. We selectively outsource the remaining 25%, mostly from Asia. We

carefully select our sourcing partners and require them to provide products according to our specifications and quality standards. We believe that strategic investments in our manufacturing facilities balanced with outsourcing from foreign and domestic suppliers will accommodate significant future sales growth and allow us to maintain an appropriate degree of control over cost, quality and service to our customers.

### **Environmental Sustainability and Social Responsibility**

We are focused on environmental and social responsibility and incorporating uniform social, environmental, health and safety programs into our manufacturing standards.

Our “green” initiatives include but are not limited to the use of responsibly harvested Appalachian woods, water-based finishes and measuring our carbon footprint, greenhouse gases and recycled materials from our operations. We have eliminated the use of heavy metals and hydrochloroflourocarbons in all packaging. Our mattresses and custom upholstery use foam made without harmful chemicals and substances. We have implemented the Enhancing Furniture’s Environmental Culture (EFEC) environmental management system sponsored by the American Home Furnishing Alliance (AHFA) at all our domestic manufacturing, distribution and service center facilities, and have expanded these efforts to our retail design centers, which have now been registered in EFEC. Our Mexico and Honduras facilities have been audited and are registered under the AHFA's EFEC program. Our domestic manufacturing, distribution and service centers have also achieved Sustainable by Design (SBD) registration status under the EFEC program. SBD provides a framework for home furnishings companies to create and maintain a corporate culture of conservation and environmental stewardship by integrating socio-economic policies and sustainable business practices into their manufacturing operations and sourcing strategies.

The Company requires its sourcing facilities that manufacture Ethan Allen branded products to implement a labor compliance program and meet or exceed the standards established for preventing child labor, involuntary labor, coercion & harassment, discrimination, and restrictions to freedom of association. These facilities must also provide a safe and healthy environment in all workspaces, compliance with all local wage and hour laws and regulations, compliance with all applicable environmental laws and regulations, and they must authorize Ethan Allen and/or its designated agents (including third-party auditing companies) to engage in monitoring activities to confirm compliance.

We work to ensure our products are safe in our customers’ homes through responsible use of chemicals and manufacturing substances.

### **Raw Materials and Other Suppliers**

The most important raw materials we use in furniture manufacturing are lumber, veneers, plywood, hardware, glue, finishing materials, glass, laminates, steel, fabrics, foam, and filling material. The various types of wood used in our products include cherry, ash, oak, maple, prima vera, African mahogany, birch, rubber wood and poplar.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

Fabrics and other raw materials are purchased both domestically and outside the United States. We have no significant long-term supply contracts, and have sufficient alternate sources of supply to prevent disruption in supplying our operations. We maintain a number of sources for our raw materials, which we believe contribute to our ability to obtain competitive pricing. Lumber prices and availability fluctuate over time based on factors such as weather and demand. The cost of some of our raw materials such as foam and shipping costs are dependent on petroleum cost. Higher material prices, cost of petroleum, and costs of sourced products could have an adverse effect on margins.

Appropriate amounts of lumber and fabric inventory are typically stocked to maintain adequate production levels. We believe that our sources of supply for these materials are sufficient and that we are not dependent on any one supplier.

We enter into standard purchase agreements with certain foreign and domestic suppliers to source selected products. The terms of these arrangements are customary for the industry and do not contain any long-term contractual obligations on our behalf. We believe we maintain good relationships with our suppliers.

### **Distribution and Logistics**

We distribute our products through three distribution centers, owned by the Company, strategically located in New Jersey, Oklahoma, and Virginia. These distribution centers provide efficient cross-dock operations to receive and ship product from our manufacturing facilities and third-party suppliers to our retail network of Company and independently operated retail service centers. Retail service centers prepare products for delivery into clients' homes. At June 30, 2018, the Company operated retail design centers were supported by 14 Company operated retail service centers and 15 service centers operated by third parties.

While we manufacture to custom order the majority of our products, we also stock selected case goods, upholstery and home accents to provide for quick delivery of in-stock items and to allow for more efficient production runs. We utilize independent carriers to ship our products.

Our practice has been to sell our products at the same delivered cost to all Company and independently operated design centers in North America, regardless of their shipping point. This policy creates pricing credibility with our wholesale customers while providing our retail segment the opportunity to achieve more consistent margins by removing fluctuations attributable to the cost of shipping. Further, this policy eliminates the need for our independent retailers to carry significant amounts of inventory in their own warehouses. As a result, we obtain more accurate

consumer product demand information.

### **Marketing Programs**

Our multifaceted, multichannel marketing and advertising strategies drive traffic both to design centers and our digital mediums. We believe these efforts give us a strong competitive advantage in the home furnishings industry while benefiting our worldwide retail network of approximately 300 design centers as well as the independent members of our Interior Design Affiliate program.

Our team of advertising specialists work to position Ethan Allen as an authority on design, a leader in exemplary service, and a source of style for everyone. In our marketing campaigns, we capitalize on Ethan Allen's strong brand equity, finding creative and compelling ways to promote our tremendous range of products, services, special programs, and custom options. We deliver these messages in a variety of ways – locally, nationally, and globally – to connect and engage with our target audience and drive sales.

As digital channels have taken on increasing importance, we continue to expand our digital marketing reach – supplementing traditional advertising strategies. Our channels include digital and social media, national and local television, direct mail, national and local newspapers, local and satellite radio, and local shelter magazines. Additionally, our robust email marketing program delivers inspiration, sales messages, design solutions, and product information to an ever-expanding database of current and potential clients.

Our direct mail magazine, which emphasizes the breadth of our products and services, is one of Ethan Allen's key marketing tools. We produce these magazines multiple times a year; in fiscal 2018, we distributed approximately 17 million copies. We distribute them to targeted marketing segments based on data collected internally and through independent market research. We continually refine our direct mail marketing lists to target clients and potential clients who are most likely to purchase, which provides better returns on direct mail expenditures.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

Our websites – ethanallen.com and ethanallen.ca – undergo continuous conversion optimization to boost sales as clients shop, design, and purchase. We also have a web presence to support our international licensees – in some cases, using local languages; in all cases, linking back to ethanallen.com. These websites position Ethan Allen in a manner consistent with our brand yet specific to the region.

A robust and informative Extranet connects our retail network, keeping the lines of communication open among our retailers, design professionals, merchandisers, trainers, and corporate personnel. Information about every aspect of Ethan Allen's retail business is shared here, including advertising materials, prototype floor plan displays, and extensive product details.

### **Retail Design Centers**

Ethan Allen design centers are typically located in busy retail settings as freestanding destinations or as part of town centers, lifestyle centers, suburban strip malls or shopping malls, depending upon the real estate opportunities in a particular market. Our design centers average approximately 15,000 square feet in size with 46% between 15,000 and 25,000 square feet and 50% less than or equal to 15,000 square feet and 4% greater than 25,000 square feet.

Combining technology with personal service in our design centers has allowed us to reduce the size of our design centers. As of June 30, 2018 we operated 18 new design centers that have opened in the past three years, and these average 9,300 square feet. These smaller footprint design centers reflect our direction as we move forward in repositioning our retail design centers. These new and relocated design centers also reflect our shift from destination and shopping mall locations to lifestyle centers that better project our brand and offer increased traffic opportunities.

We strive to maintain consistency of presentation throughout our retail design centers through a comprehensive set of standards and display planning assistance. These interior display design standards assist each design center in presenting a high quality image by using focused lifestyle settings and select product category groupings to display our products and information to facilitate design solutions and to educate consumers. We also create a consistent brand projection through our exterior facades and signage. The establishment of these standards has helped position Ethan Allen as a leader in the home furnishings industry.

We continue to strengthen the Ethan Allen brand with many initiatives, including the opening of new and relocating design centers in desirable locations, updating presentations and floor plans, strengthening of the professionalism of

our designers through training and certification, and the consolidation of certain design centers and service centers.

### **People**

At June 30, 2018 and June 30, 2017, the Company, through its subsidiaries, had approximately 5,200 employees. The majority of our employees are employed on a fulltime basis and we believe we maintain good relationships with our employees, none of whom are represented by unions.

### **Customer Service Offerings**

We offer numerous customer service programs, each of which has been developed and introduced to consumers in an effort to make their shopping experience easier and more enjoyable.

#### ***Gift Card***

This program allows customers to purchase and redeem gift cards through our website or at any participating retail design center, which can be used for any of our products or services.

#### ***Ethan Allen Consumer Credit Programs***

The Ethan Allen Platinum program offers consumers (clients) a menu of custom financing options. Financing offered through this program is administered by a third-party financial institution and is granted to our customers on a non-recourse basis to the Company. Clients may apply for an Ethan Allen Platinum card at any participating design center or on-line at [ethanallen.com](http://ethanallen.com).

### **Competition**

We believe the home furnishings industry competes primarily on the basis of product styling and quality, personal service, prompt delivery, product availability and price. We further believe that we effectively compete on the basis of each of these factors and that, more specifically, our complimentary interior design service, direct manufacturing, product presentations, and website create a distinct competitive advantage, further supporting our mission of



providing consumers with a complete home decorating and design solution. We also believe that we differentiate ourselves further with the quality of our interior design service through our intensive training. Our objective is to continue to develop and strengthen our retail network by (i) expanding the Company operated retail business through the repositioning of and opening of new design centers, (ii) obtaining and retaining independent retailers, encouraging such retailers to expand their business through the opening or relocation of new design centers with the objective of increasing the volume of their sales, (iii) further expanding our sales network through our IDA and realtor referral programs and (iv) further expanding our ecommerce.

The internet provides a highly competitive medium for the sale of a significant amount of home furnishings each year, and we believe it is becoming increasingly important. Much of that product is sold through commodity oriented, low priced and low service retailers. We believe consumers are spending more time researching on the internet and are thus better informed when they do visit our brick and mortar facilities. At Ethan Allen our internet strategy is to drive traffic into our design centers by combining technology with excellent personal service. Though our customers have the opportunity to buy our products on-line, we take the process further. With so much of our product customizable, we encourage our website customers to get personal help from our interior design professionals either in person or by chatting on-line with one of our qualified design consultants. This complimentary direct contact with one of our knowledgeable interior designers creates a competitive advantage through our excellent personal service. This enhances the online experience and regularly leads to internet customers becoming clients of our network of interior design centers.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

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### **Trademarks**

We currently hold, or have registration applications pending for, numerous trademarks, service marks and copyrights for the Ethan Allen name, logos and designs in a broad range of classes for both products and services in the United States and in many foreign countries. In addition, we have registered, or have applications pending for certain of our slogans utilized in connection with promoting brand awareness, retail sales and other services and certain collection names. We view such trademarks and service marks as valuable assets and have an ongoing program to diligently monitor and defend, through appropriate action, against their unauthorized use.

### **Executive Officers of the Registrant**

Set forth in the table below is a list of our executive officers, together with certain biographical information, including their ages as of the date of this Report:

M. Farooq Kathwari, age 73

Chairman of the Board, President and Chief Executive Officer since 1988

Kathy Bliss, age 54

Senior Vice-President, Retail since October 2017

Vice-President, Retail since August 2013

Daniel M. Grow, age 72

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Senior Vice President, Business Development since February 2015  
Vice-President, Business Development from 2009 to 2015

Eric D. Koster, age 71  
Vice-President, General Counsel and Secretary since April 2013  
Private practice prior to joining the Company in April 2013

Tracy Paccione, age 52  
Senior Vice-President, Merchandising since July 2017  
Vice-President, Merchandising since June 2009

Christopher Robertson, age 49  
Vice President, Logistics and Service since January 2016  
Director, Operations Support since May 2011

Clifford Thorn, age 66  
Vice-President, Upholstery Manufacturing since May 2001

Corey Whitely, age 58  
Executive Vice-President, Administration, Chief Financial Officer and Treasurer since July 2014  
Executive Vice-President, Operations from October 2007 through July 2014

Michael Worth, age 51  
Vice-President, Case Goods Manufacturing since December 2016  
Regional Operations Manager, Case Goods since February 2004

**Item 1A. Risk Factors**

*The following information describes certain significant risks and uncertainties inherent in our business that should be carefully considered, along with other information contained elsewhere in this Annual Report and in other filings, when making an investment decision with respect to us. If one or more of these risks occurs, the impact on our business, including our financial condition, results of operations, and cash flows could be adverse.*

***Competition from overseas manufacturers and domestic retailers may adversely affect our business, operating results or financial condition.***

Our wholesale business segment is involved in the development of our brand, which encompasses the design, manufacture, sourcing, sales and distribution of our home furnishings products, and competes with other U.S. and

foreign manufacturers. Our retail network sells home furnishings to consumers through a network of independently operated and Company operated design centers, and competes against a diverse group of retailers ranging from specialty stores to traditional furniture and department stores, any of which may operate locally, regionally, nationally or globally, as well as over the internet. We also compete with these and other retailers for appropriate retail locations as well as for qualified design consultants and management personnel. Such competition could adversely affect our future financial performance.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

Industry globalization has led to increased competitive pressures brought about by the increasing volume of imported finished goods and components, particularly for case good products, and the development of manufacturing capabilities in other countries, specifically within Asia. The increase in overseas production has created over capacity for many manufacturers, including us, which has led to industry wide plant consolidation. In addition, because many foreign manufacturers are able to maintain substantially lower production costs, including the cost of labor and overhead, imported product may be capable of being sold at a lower price to consumers, which, in turn, could lead to some measure of further industry wide price deflation.

We cannot provide assurance that we will be able to establish or maintain relationships with sufficient or appropriate manufacturers, whether foreign or domestic, to supply us with selected case goods, upholstery and home accent items to enable us to maintain our competitive advantage. In addition, the emergence of foreign manufacturers has served to broaden the competitive landscape. Some of these competitors produce furniture types not manufactured by us and may have greater financial resources available to them or lower costs of operating. This competition could adversely affect our future financial performance.

***Failure to successfully anticipate or respond to changes in consumer tastes and trends in a timely manner could adversely impact our business, operating results and financial condition.***

Sales of our products are dependent upon consumer acceptance of our product designs, styles, quality and price. We continuously monitor changes in home design trends through attendance at international industry events and fashion shows, internal marketing research, and regular communication with our retailers and design consultants who provide valuable input on consumer tendencies. However, as with all retailers, our business is susceptible to changes in consumer tastes and trends. Such tastes and trends can change rapidly and any delay or failure to anticipate or respond to changing consumer tastes and trends in a timely manner could adversely impact our business, operating results and financial condition.

***Our success depends upon our brand, marketing and advertising efforts and pricing strategies. If we are not able to maintain and enhance our brand, or if we are not successful in these other efforts, our business and operating results could be adversely affected.***

Maintaining and enhancing our brand is critical to our ability to expand our base of customers and may require us to make substantial investments. Our advertising campaign utilizes television, direct mail, digital, newspapers, magazines and radio to maintain and enhance our existing brand equity. We cannot provide assurance that our marketing, advertising and other efforts to promote and maintain awareness of our brand will not require us to incur

substantial costs. If these efforts are unsuccessful or we incur substantial costs in connection with these efforts, our business, operating results and financial condition could be adversely affected.

***We face changes in global and local economic conditions that may adversely affect consumer demand and spending, our manufacturing operations or sources of merchandise and international operations.***

Historically, the home furnishings industry has been subject to cyclical variations in the general economy and to uncertainty regarding future economic prospects. Such uncertainty, as well as other variations in global economic conditions such as rising fuel costs, wage and benefit inflation, currency fluctuations, and increasing interest rates, may continue to cause inconsistent and unpredictable consumer spending habits, while increasing our own input costs. These risks, as well as industrial accidents or work stoppages, could also severely disrupt our manufacturing operations, which could have a material adverse effect on our financial performance.

We import a portion of our merchandise from foreign countries and operate manufacturing plants in Mexico and Honduras and operate retail design centers in Canada. As a result, our ability to obtain adequate supplies or to control our costs may be adversely affected by events affecting international commerce and businesses located outside the United States, including natural disasters, changes in international trade, central bank actions, changes in the relationship of the U.S. dollar versus other currencies, labor availability and cost, and other governmental policies of the U.S. and the countries from which we import our merchandise or in which we operate facilities. The inability to import products from certain foreign countries or the imposition of significant tariffs could have a material adverse effect on our results of operations.

***The Company's business may be adversely affected by changes in U.S. policy related to imported merchandise.***

A significant amount of the Company's merchandise is sourced from outside of the United States. The U.S. government is considering proposals for substantial changes to its trade and tax policies, which could include import restrictions, increased import tariffs, changes to or withdrawal from existing trade agreements, and border-adjustment taxes among other possible measures. Material changes in these policies could increase the Company's tax obligations or require the Company to increase prices to customers, which would likely adversely affect sales. Any significant change in U.S. policy related to imported merchandise could have a material adverse effect on the Company's business and financial results.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

***An economic downturn may materially adversely affect our business.***

Our business and results of operations are affected by international, national and regional economic conditions. Regional economic conditions in the United States and in other regions of the world where we have a concentration of design centers such as Canada or China may impact the Company greater compared to economic conditions in other parts of the world where we have lesser concentration of design centers. An economic downturn of significance or extended duration could adversely affect consumer demand and discretionary spending habits and, as a result, our business performance, profitability, and cash flows.

***Our business may be materially affected by changes to fiscal and tax policies. Potentially negative or unexpected tax consequences of these policies, or the uncertainty surrounding their potential effects, could adversely affect our results of operations and share price.***

The U.S. Tax Cuts and Jobs Act of 2017 (the “TCJA”) was approved by the U.S. Congress on December 20, 2017 and signed into law on December 22, 2017. This legislation makes significant changes to the U.S. Internal Revenue Code of 1986, as amended (the “IRC”). Such changes include a reduction in the corporate tax rate from 35% to 21% and limitations on certain corporate deductions and credits, among other changes. In addition, the TCJA requires complex computations to be performed that were not previously required in U.S. tax law, significant judgments to be made in interpretation of the provisions of the TCJA and significant estimates in calculations, and the preparation and analysis of information not previously relevant or regularly produced.

While we have provided for the effect of the TCJA in our Consolidated Financial Statements the final impacts of the TCJA could be materially different from our expectations. For example, adverse changes in the underlying profitability and financial outlook of our operations or changes in tax law could lead to changes in our valuation allowances against deferred tax assets on our consolidated balance sheets, which could materially affect our results of operations. The U.S. Treasury Department, the Internal Revenue Service (the “IRS”), and other standard-setting bodies could interpret or issue guidance on how provisions of the TCJA will be applied or otherwise administered that is different from our interpretation. Finally, foreign governments may enact tax laws in response to the TCJA that could result in further changes to global taxation and materially affect our financial position and results of operations. The uncertainty surrounding the effect of the reforms on our financial results and business could also weaken confidence among investors in our financial condition. This could, in turn, have a materially adverse effect on the price of our ordinary shares.

***Our number of manufacturing and logistics sites may increase our exposure to business disruptions and could result in higher transportation costs.***

We have a limited number of manufacturing sites in our case goods and upholstery operations, consolidated our distribution network into fewer centers for both wholesale and retail segments, and operate a single home accents plant. Our upholstery operations consist of three upholstery plants at our North Carolina campus and one plant in Mexico. The Company operates three manufacturing plants (North Carolina, Vermont, and Honduras) and one sawmill in support of our case goods operations. Our plants require various raw materials and commodities such as logs and lumber for our case goods plants and foam, springs and engineered hardwood board for our upholstery plants. As a result of the consolidation of our manufacturing operations into fewer facilities, if any of our manufacturing or logistics sites experience significant business interruption, our ability to manufacture or deliver our products in a timely manner would likely be impacted. While we have long standing relationships with multiple outside suppliers of our raw materials and commodities, there can be no assurance of their ability to fulfill our supply needs on a timely basis. The consolidation to fewer locations has resulted in longer distances for delivery and could result in higher costs to transport products if fuel costs increase significantly.

***Fluctuations in the price, availability and quality of raw materials could result in increased costs or cause production delays which might result in a decline in sales, either of which could adversely impact our earnings.***

We use various types of wood, foam, fibers, fabrics, leathers, and other raw materials in manufacturing our furniture. Certain of our raw materials, including fabrics, are purchased domestically and outside North America. Fluctuations in the price, availability and quality of raw materials could result in increased costs or a delay in manufacturing our products, which in turn could result in a delay in delivering products to our customers. For example, lumber prices fluctuate over time based on factors such as weather and demand, which in turn, impact availability. Production delays or upward trends in raw material prices could result in lower sales or margins, thereby adversely impacting our earnings.

In addition, certain suppliers may require extensive advance notice of our requirements in order to produce products in the quantities we desire. This long lead time may require us to place orders far in advance of the time when certain products will be offered for sale, thereby exposing us to risks relating to shifts in consumer demand and trends, and any significant downturn in the U.S. economy.



## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

***Our current and former manufacturing and retail operations and products are subject to increasingly stringent environmental, health and safety requirements.***

We use and generate hazardous substances in our manufacturing and retail operations. In addition, both the manufacturing properties on which we currently operate and those on which we have ceased operations are and have been used for industrial purposes. Our manufacturing operations and, to a lesser extent, our retail operations involve risk of personal injury or death. We are subject to increasingly stringent environmental, health and safety laws and regulations relating to our products, current and former properties and our current operations. These laws and regulations provide for substantial fines and criminal sanctions for violations and sometimes require product recalls and/or redesign, the installation of costly pollution control or safety equipment, or costly changes in operations to limit pollution or decrease the likelihood of injuries. In addition, we may become subject to potentially material liabilities for the investigation and cleanup of contaminated properties and to claims alleging personal injury or property damage resulting from exposure to or releases of hazardous substances or personal injury because of an unsafe workplace.

In addition, noncompliance with, or stricter enforcement of, existing laws and regulations, adoption of more stringent new laws and regulations, discovery of previously unknown contamination or imposition of new or increased requirements could require us to incur costs or become the basis of new or increased liabilities that could be material.

***The Company's sales and operating results could be adversely affected by product safety concerns.***

If the Company's merchandise offerings do not meet applicable safety standards or consumers' expectations regarding safety, the Company could experience decreased sales, increased costs and/or be exposed to legal and reputational risk. Events that give rise to actual, potential or perceived product safety concerns could expose the Company to government enforcement action and/or private litigation. Reputational damage caused by real or perceived product safety concerns could negatively affect the Company's business and results of operations.

***The Company relies heavily on information and technology to operate its business, and any disruption to its technology infrastructure (including cyber attacks) or the internet could harm the Company's operations.***

In the current environment, there are numerous and evolving risks to cybersecurity and privacy, including criminal hackers, hacktivists, state-sponsored intrusions, industrial espionage, employee malfeasance and human or technological error. High-profile security breaches at other companies and in government agencies have increased in

recent years, and security industry experts and government officials have warned about the risks of hackers and cyberattacks targeting businesses such as ours. Computer hackers and others routinely attempt to breach the security of technology products, services and systems, and to fraudulently induce employees, customers, or others to disclose information or unwittingly provide access to systems or data. We operate many aspects of our business including financial reporting, and customer relationship management through server and web based technologies, and store various types of data on such servers or with third parties who in turn store it on servers and in the “cloud”. Any disruption to the internet or to the Company's or its service providers' global technology infrastructure, including malware, insecure coding, “Acts of God,” attempts to penetrate networks, data theft or loss and human error, could have adverse effects on the Company's operations. A cyber attack of our systems or networks that impairs our information technology systems could disrupt our business operations and result in loss of service to customers. The risk of cyberattacks to our Company also includes attempted breaches of contractors, business partners, vendors and other third parties. We have a comprehensive cybersecurity program designed to protect and preserve the integrity of our information technology systems. We have experienced and expect to continue to experience actual or attempted cyber attacks of our IT systems or networks; however, none of these actual or attempted cyber attacks had a material impact on our operations or financial condition.

Additionally, we have access to sensitive customer information in the ordinary course of business. If a significant data breach occurred, our reputation may be adversely affected, customer confidence may be diminished, or we may be subject to legal claims, or legal proceedings, including regulatory investigations and actions, may have a negative impact on our reputation, may lead to regulatory enforcement actions against us, and may materially adversely affect our business, operating results and financial condition. The loss, disclosure or misappropriation of our business information may materially adversely affect our business, operating results and financial condition. Further, legislative or regulatory action in these areas is evolving, and we may be unable to adapt our IT systems or to manage the IT systems of third parties to accommodate these changes. Finally, if a significant data breach occurred, our reputation could be materially and adversely affected, confidence among our customers may be diminished.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

While we have invested and continue to invest in information technology risk management, cybersecurity and disaster recovery plans, these measures cannot fully insulate the Company from technology disruptions or data theft or loss and the resulting adverse effect on the Company's operations and financial results.

***Our business is sensitive to increasing labor costs, competitive labor markets, our continued ability to retain high quality personnel and risks of work stoppages.***

The market for qualified employees and personnel in the retail and manufacturing industries is highly competitive. Our success depends upon our ability to attract, retain and motivate qualified artisans, professional and clerical employees and upon the continued contributions of these individuals. We cannot provide assurance that we will be successful in attracting and retaining qualified personnel. A shortage of qualified personnel may require us to enhance our wage and benefits package in order to compete effectively in the hiring and retention of qualified employees. Our labor and benefit costs may continue to increase and such increases may not be recovered. This could have a material adverse effect on our business, operating results and financial condition.

***We depend on key personnel and could be affected by the loss of their services.***

The success of our business depends upon the services of certain senior executives, and in particular, the services of M. Farooq Kathwari, Chairman of the Board, President and Chief Executive Officer, who is the only one of our senior executives who operates under a written employment agreement. The loss of any such person or other key personnel could have a material adverse effect on our business and results of operations.

***We may be unable to obtain sufficient external funding to finance our operations and growth.***

Historically, we have relied upon our cash from operations to fund our debt service, operations and growth. As we operate and expand our business, we may rely on external funding sources, including the proceeds from the issuance of additional debt or use of the \$115 million revolving bank line of credit under our existing credit facility. The credit facility bears interest at a floating rate and there is a risk that the rate will increase and as we are not hedging our interest rate for the credit facility, our debt service costs could increase. Any unexpected reduction in cash flow from operations could increase our external funding requirements to levels above those currently available. There can be no assurance that we will not experience unexpected cash flow shortfalls in the future or that any increase in external funding required by such shortfalls will be available on acceptable terms or at all.

***Access to consumer credit could be interrupted and reduce sales and profitability.***

Our ability to continue to access consumer credit for our clients could be negatively affected by conditions outside our control. If capital market conditions have a material negative change, there is a risk that our business partner that issues our private label credit card program may not be able to fulfill its obligations under that agreement. In addition, the tightening of credit markets may restrict the ability and willingness of customers to make purchases.

***Operating losses could reduce our liquidity and impact our dividend policy.***

Historically, we have relied on our cash from operations or debt issuances to fund our operations and the payment of cash dividends. If the Company's financial performance were to deteriorate resulting in financial losses we may not be able to fund a shortfall from operations and would require external funding. Some financing instruments used by the Company historically may not be available to the Company in the future. We cannot assure that additional sources of financing would be available to the Company on commercially favorable terms should the Company's capital requirements exceed cash available from operations and existing cash and cash equivalents. In such circumstances, the Company may reduce its quarterly dividends.

***Additional impairment charges could reduce our profitability.***

We have significant long lived tangible and intangible assets recorded on our balance sheets. If our operating results decline, we may incur impairment charges in the future, which could have a material impact on our financial results. We evaluate the recoverability of the carrying amount of our long lived tangible and intangible assets on an ongoing basis. There can be no assurance that the outcome of such future reviews will not result in substantial impairment charges. Impairment assessment inherently involves judgments as to assumptions about expected future cash flows and the impact of market conditions on those assumptions. Future events and changing market conditions may impact our assumptions as to prices, costs or other factors that may result in changes in our estimates of future cash flows. Although we believe the assumptions we use in testing for impairment are reasonable, significant changes in any of our assumptions could produce a significantly different result.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

*We may not be able to maintain our current design center locations at current costs. We may also fail to successfully select and secure design center locations.*

Our design centers are typically located in busy urban settings as freestanding destinations or as part of suburban strip malls or shopping malls, depending upon the real estate opportunities in a particular market. Our business competes with other retailers and as a result, our success may be affected by our ability to renew current design center leases and to select and secure appropriate retail locations for existing and future design centers.

*Our results of operations for any quarter are not necessarily indicative of our results of operations for a full year.*

Sales of furniture and other home furnishing products fluctuate from quarter to quarter due to such factors as changes in global and regional economic conditions, changes in competitive conditions, changes in production schedules in response to seasonal changes in energy costs and weather conditions, changes in consumer order patterns, and the timing of various promotional events. From time to time, we have experienced, and may continue to experience, volatility with respect to demand for our home furnishing products. Accordingly, results of operations for any quarter are not necessarily indicative of the results of operations for a full year.

*Failure to protect our intellectual property could adversely affect us.*

We believe that our copyrights, trademarks, service marks, trade secrets, and all of our other intellectual property are important to our success. We rely on patent, trademark, copyright and trade secret laws, and confidentiality and restricted use agreements, to protect our intellectual property and may seek licenses to intellectual property of others. Some of our intellectual property is not covered by any patent, trademark, or copyright or any applications for the same. We cannot provide assurance that agreements designed to protect our intellectual property will not be breached, that we will have adequate remedies for any such breach, or that the efforts we take to protect our proprietary rights will be sufficient or effective. Any significant impairment of our intellectual property rights or failure to obtain licenses of intellectual property from third parties could harm our business or our ability to compete. Moreover, we cannot provide assurance that the use of our technology or proprietary know how or information does not infringe the intellectual property rights of others. If we have to litigate to protect or defend any of our rights, such litigation could result in significant expense.

### **Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

Our 144,000 sq. ft. corporate headquarters, located in Danbury, Connecticut, and adjacent Ethan Allen Hotel and Conference Center, containing approximately 200 guestrooms, are owned by the Company. The hotel is used primarily for functions and accommodations for the general public as well as in connection with Ethan Allen functions and training programs.

We operate nine manufacturing facilities located in the U.S., Mexico and Honduras. These facilities are owned by the Company and include four case goods plants (including one sawmill) totaling 1,789,000 square feet, four upholstery furniture plants totaling 1,261,000 square feet, and one home accent plant of 177,000 square feet. Our wholesale division also owns and operates three national distribution and fulfillment centers, one of which shares a facility with our manufacturing, which are a combined 1,001,000 square feet. Two of our case goods manufacturing facilities are located in Vermont, one is in North Carolina and one is in Honduras. We have three upholstery manufacturing facilities at our North Carolina campus, and one in Mexico. Our home accents plant is located in New Jersey, and our distribution facilities are located in New Jersey, Oklahoma, and Virginia.

We own three and lease 11 retail service centers, totaling approximately 775,000 square feet. Our retail service centers are located throughout the United States and Canada and serve to support our various retail sales districts.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

The location activity and geographic distribution of our retail network for fiscal years ended June 30 are as follows:

|                                            | Fiscal 2018           |                  |       | Fiscal 2017           |                  |       |
|--------------------------------------------|-----------------------|------------------|-------|-----------------------|------------------|-------|
|                                            | Independent-retailers | Company-operated | Total | Independent-retailers | Company-operated | Total |
| Retail Design Center location activity:    |                       |                  |       |                       |                  |       |
| Balance at beginning of period             | 155                   | 148              | 303   | 153                   | 143              | 296   |
| New locations                              | 11                    | 3                | 14    | 8                     | 6                | 14    |
| Closures                                   | (11 )                 | (5 )             | (16 ) | (5 )                  | (2 )             | (7 )  |
| Transfers                                  | (2 )                  | 2                | -     | (1 )                  | 1                | -     |
| Balance at end of period                   | 153                   | 148              | 301   | 155                   | 148              | 303   |
| Relocations (in new and closures)          | 0                     | 1                | 1     | 1                     | 2                | 3     |
| Retail Design Center geographic locations: |                       |                  |       |                       |                  |       |
| United States                              | 44                    | 142              | 186   | 48                    | 142              | 190   |
| Canada                                     | -                     | 6                | 6     | -                     | 6                | 6     |
| China                                      | 87                    | -                | 87    | 82                    | -                | 82    |
| Other Asia                                 | 9                     | -                | 9     | 12                    | -                | 12    |
| Europe                                     | 6                     | -                | 6     | 6                     | -                | 6     |
| Middle East                                | 7                     | -                | 7     | 7                     | -                | 7     |
| Total                                      | 153                   | 148              | 301   | 155                   | 148              | 303   |

Of the 148 Company operated retail design centers, 50 of the properties are owned and 98 are leased. We own one and lease six additional retail properties, which we lease to three independent Ethan Allen retailers, and four unaffiliated third parties. See Note 7 to the Consolidated Financial Statements included under Item 8 of this Annual Report for more information with respect to our operating lease obligations.

We believe that all our properties are well maintained and in good condition. We estimate that our manufacturing plants are currently operating at approximately 54% of capacity based on their current shifts and staffing. We believe we have additional capacity at selected facilities, which we could utilize with minimal additional capital expenditures.

**Item 3. Legal Proceedings**

In the ordinary course of our business, we are party to various legal proceedings and claims which we believe are incidental to the operation of our business. Other than as described under Note 13 to our consolidated financial statements included in Part II, Item 8 of this Annual Report on Form 10-K, we believe the ultimate outcome of these proceedings to which we are currently a party will not have a material adverse effect on our business, financial position, results of operations or cash flows.

Regulations issued under the Clean Air Act Amendments of 1990 required the industry to reformulate certain furniture finishes or institute process changes to reduce emissions of volatile organic compounds. Compliance with many of these requirements has been facilitated through the introduction of high solids coating technology and alternative formulations. In addition, we have instituted a variety of technical and procedural controls, including reformulation of finishing materials to reduce toxicity, implementation of high velocity low pressure spray systems, development of storm water protection plans and controls, and further development of related inspection/audit teams, all of which have served to reduce emissions per unit of production. We remain committed to implementing new waste minimization programs and/or enhancing existing programs with the objective of (i) reducing the total volume of waste, (ii) limiting the liability associated with waste disposal, and (iii) continuously improving environmental and job safety programs on the factory floor which serve to minimize emissions and safety risks for employees. To reduce the use of hazardous materials in the manufacturing process, we will continue to evaluate the most appropriate, cost-effective control technologies for finishing operations and production methods. We believe that our facilities are in material compliance with all such applicable laws and regulations. Our currently anticipated capital expenditures for environmental control facility matters are not material.



## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

### **Item 4. Mine Safety Disclosures**

Not applicable.

## **PART II**

### **Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Our common stock is traded on the New York Stock Exchange ("NYSE") under ticker symbol "ETH". The following table sets forth, for each quarterly period during the past two fiscal years, (i) the intraday high and low sales prices of our common stock as reported on the NYSE and (ii) the dividends per share declared by us:

|                           | Market Price |         | Dividends |
|---------------------------|--------------|---------|-----------|
|                           | High         | Low     | Per Share |
| <b><u>Fiscal 2018</u></b> |              |         |           |
| First Quarter             | \$33.12      | \$27.35 | 0.19      |
| Second Quarter            | 32.90        | 26.45   | 0.50      |
| Third Quarter             | 29.40        | 22.15   | 0.19      |
| Fourth Quarter            | 25.15        | 21.50   | 0.19      |
| <b><u>Fiscal 2017</u></b> |              |         |           |
| First Quarter             | \$36.77      | \$30.63 | 0.17      |
| Second Quarter            | 38.80        | 29.20   | 0.19      |
| Third Quarter             | 37.90        | 27.75   | 0.19      |
| Fourth Quarter            | 32.50        | 26.75   | 0.19      |

As of July 26, 2018, there were 222 shareholders of record of our common stock. Management estimates there are approximately 9,000 beneficial shareholders of the Company's common stock. The Company's policy is to issue quarterly dividends, and we expect to continue to declare quarterly dividends for the foreseeable future, business conditions permitting.

**Equity Compensation Plan Information**

The Equity Compensation Plan Information required by this Item will appear in the Ethan Allen Interiors Inc. proxy statement for the 2018 Annual Meeting of Shareholders and is incorporated herein by reference in the introductory paragraph of Part III of this Annual Report.

**Issuer Purchases of Equity Securities**

During the fiscal year ended June 30, 2018 the Company repurchased 950,484 shares of our common stock at an average price of \$23.17 per share. Certain information regarding purchases of our common stock made by us during the three months ended June 30, 2018 is as follows:

| <u>Period</u> | Number<br>of<br>Shares<br>Purchased | Average<br>Price<br>Paid<br>Per<br>Share | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number of<br>Shares that<br>May Yet<br>Be<br>Purchased<br>Under the<br>Plans or<br>Programs |
|---------------|-------------------------------------|------------------------------------------|----------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------|
| April 2018    | 513,619                             | \$ 22.53                                 | 513,619                                                                                                  | 2,954,911                                                                                              |
| May 2018      | 436,865                             | \$ 23.91                                 | 436,865                                                                                                  | 2,518,046                                                                                              |
| June 2018     | -                                   | \$ -                                     | -                                                                                                        | 2,518,046                                                                                              |
| Total         | 950,484                             | \$ 23.17                                 | 950,484                                                                                                  |                                                                                                        |

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

On November 21, 2002, our Board of Directors approved a share repurchase program authorizing us to repurchase up to 2,000,000 shares of our common stock, from time to time, either directly or through agents, in the open market at prices and on terms satisfactory to us. Subsequent to that date, the Board of Directors increased the aggregate authorization under the repurchase program on several separate occasions, the last of which was on April 24, 2018 when the Board of Directors increased the aggregate authorization to approximately 3,000,000 shares. There is no expiration date on the repurchase authorization and the amount and timing of future share repurchases, if any, will be determined as market and business conditions warrant.

### **Comparative Company Performance**

The following line graph compares the cumulative total stockholder return for the Company with the S&P 500 Index, and the S&P Retail Select Industry Index (SPSIRE), assuming \$100 was invested on June 30, 2013.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES****Item 6. Selected Financial Data**

The following table presents selected financial data for the fiscal years ended June 30, 2014 through 2018 that has been derived from our consolidated financial statements. The information set forth below should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included under Item 7 of this Annual Report and our Consolidated Financial Statements (including the notes thereto) included under Item 8 of this Annual Report. Dollar amounts are in thousands except per share data.

|                                                     | Fiscal Year Ended June 30, |           |           |           |           |
|-----------------------------------------------------|----------------------------|-----------|-----------|-----------|-----------|
|                                                     | 2018                       | 2017      | 2016      | 2015      | 2014      |
| <b><u>Consolidated Operations Data</u></b>          |                            |           |           |           |           |
| Net Sales                                           | \$766,784                  | \$763,385 | \$794,202 | \$754,600 | \$746,659 |
| Cost of Sales                                       | 350,820                    | 343,662   | 351,966   | 343,437   | 340,163   |
| Selling, general and administrative expenses        | 367,097                    | 361,773   | 353,057   | 345,229   | 336,860   |
| Operating income                                    | 48,867                     | 57,950    | 89,179    | 65,934    | 69,636    |
| Interest and other expense, net                     | (200 )                     | 955       | 1,223     | 9,251     | 7,234     |
| Income before income tax expense                    | 49,067                     | 56,995    | 87,956    | 56,683    | 62,402    |
| Income tax expense (benefit)                        | 12,696                     | 20,801    | 31,319    | 19,541    | 19,471    |
| Net income                                          | \$36,371                   | \$36,194  | \$56,637  | \$37,142  | \$42,931  |
| <b><u>Per Share Data</u></b>                        |                            |           |           |           |           |
| Net income per basic share                          | \$1.33                     | \$1.31    | \$2.02    | \$1.29    | \$1.48    |
| Basic weighted average shares outstanding           | 27,321                     | 27,679    | 28,072    | 28,874    | 28,918    |
| Net income per diluted share                        | \$1.32                     | \$1.29    | \$2.00    | \$1.27    | \$1.47    |
| Diluted weighted average shares outstanding         | 27,625                     | 27,958    | 28,324    | 29,182    | 29,276    |
| Cash dividends per share                            | \$1.07                     | \$0.74    | \$0.62    | \$0.50    | \$0.40    |
| <b><u>Other Information</u></b>                     |                            |           |           |           |           |
| Depreciation and amortization                       | \$19,831                   | \$20,115  | \$19,353  | \$19,142  | \$17,930  |
| Capital expenditures and acquisitions               | \$18,773                   | \$18,321  | \$23,132  | \$21,778  | \$19,305  |
| Working capital                                     | \$93,165                   | \$116,653 | \$124,857 | \$130,012 | \$169,582 |
| Current ratio                                       | 1.77 to 1                  | 1.92 to 1 | 2.01 to 1 | 1.92 to 1 | 2.25 to 1 |
| Effective tax rate                                  | 25.9 %                     | 36.5 %    | 35.6 %    | 34.5 %    | 31.2 %    |
| <b><u>Balance Sheet Data (at end of period)</u></b> |                            |           |           |           |           |
| Total assets                                        | \$530,433                  | \$568,222 | \$577,409 | \$605,977 | \$654,434 |
| Total debt, including capital lease obligations     | \$1,680                    | \$14,339  | \$41,838  | \$76,237  | \$130,912 |
| Shareholders' equity                                | \$383,870                  | \$400,896 | \$392,202 | \$370,535 | \$367,467 |
| Debt as a percentage of equity                      | 0.4 %                      | 3.6 %     | 10.7 %    | 20.6 %    | 35.6 %    |
| Debt as a percentage of capital                     | 0.4 %                      | 3.5 %     | 9.6 %     | 17.1 %    | 26.3 %    |



## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation**

The following discussion of financial condition and results of operations is based upon, and should be read in conjunction with, our Consolidated Financial Statements (including the notes thereto) included under Item 8 of this Annual Report.

#### **Forward-Looking Statements**

Management's discussion and analysis of financial condition and results of operations and other sections of this Annual Report on Form 10-K contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), which represent management's beliefs and assumptions concerning future events based on information currently available to us relating to our future results. Such forward-looking statements are identified in this Annual Report on Form 10-K and in documents incorporated herein by reference by use of forward-looking words such as "anticipate", "believe", "plan", "estimate", "expect", "intend", "will", "may", "continue", "project", "target", "outlook", "forecast", "guidance", and similar expressions and the neg such forward-looking words. These forward-looking statements are subject to management decisions and various assumptions about future events, and are not guarantees of future performance. Actual results could differ materially from those anticipated in the forward-looking statements due to a number of risks and uncertainties including, but not limited to: competition from overseas manufacturers and domestic retailers; our anticipating or responding to changes in consumer tastes and trends in a timely manner; our ability to maintain and enhance our brand, marketing and advertising efforts and pricing strategies; changes in global and local economic conditions that may adversely affect consumer demand and spending, our manufacturing operations or sources of merchandise and international operations; changes in U.S. policy related to imported merchandise; an economic downturn; our limited number of manufacturing and logistics sites; fluctuations in the price, availability and quality of raw materials; environmental, health and safety requirements; product safety concerns; disruption to our technology infrastructure (including cyber attacks); increasing labor costs, competitive labor markets and our continued ability to retain high-quality personnel and risks of work stoppages; loss of key personnel; our ability to obtain sufficient external funding to finance our operations and growth; access to consumer credit; the effect of operating losses on our ability to pay cash dividends; our ability to locate new design center sites and/or negotiate favorable lease terms for additional design centers or for the expansion of existing design centers; the effects of terrorist attacks or conflicts or wars involving the United States or its allies or trading partners; and those matters discussed in Items 1A and 7A of this Annual Report on Form 10-K and in our other SEC filings. Accordingly, actual circumstances and results could differ materially from those contemplated by the forward-looking statements.

Given the risks and uncertainties surrounding forward-looking statements, you should not place undue reliance on these statements. Many of these factors are beyond our ability to control or predict. Our forward-looking statements speak only as of the date of this Annual Report on Form 10-K. Other than as required by law, we undertake no obligation to update or revise forward-looking statements, whether as a result of new information, future events, or otherwise.

### **Critical Accounting Policies**

Our consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles that require, in some cases, that certain estimates and assumptions be made that affect the amounts and disclosures reported in those financial statements and the related accompanying notes. Estimates are based on currently known facts and circumstances, prior experience and other reasonable assumptions. We use our best judgment in valuing these estimates and may, as warranted, solicit external advice. Actual results could differ from these estimates, assumptions and judgments, and these differences could be material. The following critical accounting policies, some of which are impacted significantly by estimates, assumptions and judgments, affect our consolidated financial statements.

***Inventories*** – Inventories (finished goods, work in process and raw materials) are stated at the lower of cost, determined on a first-in, first-out basis, and net realizable value. Cost is determined based solely on those charges incurred in the acquisition and production of the related inventory (i.e. material, labor and manufacturing overhead costs). We estimate an inventory reserve for excess quantities and obsolete items based on specific identification and historical write-downs, taking into account future demand and market conditions. If actual demand or market conditions in the future are less favorable than those estimated, additional inventory write-downs may be required.

***Revenue Recognition*** – Revenue is recognized when all the following have occurred: persuasive evidence of a sales arrangement exists (e.g., a wholesale purchase order or retail sales order); the sales arrangement specifies a fixed or determinable sales price; title and risk of ownership has passed to the customer; no specific performance obligations remain; product is shipped or services are provided to the customer; collectability is reasonably assured. As such, revenue recognition generally occurs upon the shipment of goods to independent retailers or, in the case of Ethan Allen operated retail design centers, upon delivery to the customer. If a shipping charge is billed to customers, this is included in revenue. Recorded sales provide for estimated returns and allowances. We permit our customers to return defective products and incorrect shipments, and terms we offer are standard for the industry.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

***Impairment of Long-Lived Assets and Goodwill*** – Goodwill and other indefinite-lived intangible assets are evaluated for impairment on an annual basis during the fourth quarter of each fiscal year, and between annual tests whenever events or circumstances indicate that the carrying value of the goodwill or other intangible asset may exceed its fair value. When testing goodwill for impairment, we may assess qualitative factors for some or all of our reporting units to determine whether it is more likely than not (that is, a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount, including goodwill. Alternatively, we may bypass this qualitative assessment for some or all of our reporting units and determine whether the carrying value exceeds the fair value using a quantitative assessment.

The recoverability of long-lived assets is evaluated for impairment whenever events or changes in circumstances indicate that we may not be able to recover the carrying amount of an asset or asset group. Our assessment of recoverability determines whether the carrying value will be recovered through the expected undiscounted future cash flows resulting from the use of the asset. In the event the sum of the expected undiscounted future cash flows is less than the carrying value of the asset, an impairment loss equal to the excess of the asset's carrying value over its fair value is recorded. The long-term nature of these assets requires the estimation of cash inflows and outflows several years into the future.

The fair value of our trade name, which is the Company's only indefinite-lived intangible asset other than goodwill, is valued using the relief-from-royalty method. Significant factors used in trade name valuation are rates for royalties, future growth, and the discount rate. Royalty rates are determined using an average of recent comparable values. Future growth rates are based on market participant assumptions based on the industry in which we operate, and the discount rate is determined using the weighted average cost of capital for companies within our peer group, adjusted for specific company risk premium factors.

***Income Taxes*** – Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Additional factors that we consider when making judgments about the deferred tax valuation include tax law changes, a recent history of cumulative losses, and variances in future projected profitability.

The Company evaluates, on a quarterly basis, uncertain tax positions taken or expected to be taken on tax returns for recognition, measurement, presentation, and disclosure in its financial statements. If an income tax position exceeds a 50% probability of success upon tax audit, based solely on the technical merits of the position, the Company



recognizes an income tax benefit in its financial statements. The tax benefits recognized are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The liability associated with an unrecognized tax benefit is classified as a long-term liability except for the amount for which a cash payment is expected to be made or tax positions settled within one year. We recognize interest and penalties related to income tax matters as a component of income tax expense.

***Business Insurance Reserves*** – We have insurance programs in place to cover workers’ compensation and property/casualty claims. The insurance programs, which are funded through self-insured retention, are subject to various stop-loss limitations. We accrue estimated losses using actuarial models and assumptions based on historical loss experience. Although we believe that the insurance reserves are adequate, the reserve estimates are based on historical experience, which may not be indicative of current and future losses. In addition, the actuarial calculations used to estimate insurance reserves are based on numerous assumptions, some of which are subjective. We adjust insurance reserves, as needed, in the event that future loss experience differs from historical loss patterns.

***Other Loss Reserves*** – We have a number of other potential loss exposures incurred in the ordinary course of business such as environmental claims, product liability, litigation, tax liabilities, restructuring charges, and the recoverability of deferred income tax benefits. Establishing loss reserves for these matters requires the use of estimates and judgment with regard to maximum risk exposure and ultimate liability or realization. As a result, these estimates are often developed with our counsel, or other appropriate advisors, and are based on our current understanding of the underlying facts and circumstances. Because of uncertainties related to the ultimate outcome of these issues or the possibilities of changes in the underlying facts and circumstances, additional charges related to these issues could be required in the future.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES****Results of Operations**

In this Item 7 of this Annual Report, unless otherwise noted, all comparisons are from the fiscal year ended June 30, 2018 to the prior fiscal year ended June 30, 2017 (\$ in millions except per share amounts).

A summary of our consolidated operations for the past three fiscal years is presented in the following table.

|                                           | Fiscal years ended June 30, |        |         |        |         |        |
|-------------------------------------------|-----------------------------|--------|---------|--------|---------|--------|
|                                           | 2018                        | %      | 2017    | %      | 2016    | %      |
| Net sales                                 | \$766.8                     | 100.0% | \$763.4 | 100.0% | \$794.2 | 100.0% |
| Gross profit                              | \$416.0                     | 54.2 % | \$419.7 | 55.0 % | \$442.2 | 55.7 % |
| SG&A                                      | \$367.1                     | 47.9 % | \$361.8 | 47.4 % | \$353.1 | 44.5 % |
| Operating income                          | 48.9                        | 6.4 %  | 58.0    | 7.6 %  | 89.2    | 11.2 % |
| Net income                                | 36.4                        | 4.7 %  | 36.2    | 4.7 %  | 56.6    | 7.1 %  |
| Earnings per diluted share                | \$1.32                      |        | \$1.29  |        | \$2.00  |        |
| Net cash provided by operating activities | \$42.5                      |        | \$78.6  |        | \$58.4  |        |

A summary of changes from the preceding fiscal year are presented in the following table.

|                                           | Fiscal years ended June 30, |          |        |
|-------------------------------------------|-----------------------------|----------|--------|
|                                           | 2018                        | 2017     | 2016   |
| Net sales                                 | 0.4 %                       | (3.9 %)  | 5.2 %  |
| Operating income                          | (15.7%)                     | (35.0%)  | 35.3 % |
| Net income                                | 0.5 %                       | (36.1 %) | 52.5 % |
| Earnings per diluted share                | 2.3 %                       | (35.5 %) | 57.5 % |
| Net cash provided by operating activities | (46.0%)                     | 34.7 %   | 5.9 %  |

We have completed a major transformation of our product offerings, having refreshed over 70% of our entire product line over the past three years. During fiscal 2018 we expanded our GSA business with an award of a blanket purchase agreement for the U. S. Department of State “Worldwide Residential Furniture Program”, and partnered with Amazon to sell products through the Amazon marketplace. During the fall of 2017, we introduced Passport, a focused collection of unique artisan crafted items inspired by designs from around the world, and in the spring of 2018 launched our new Uptown collection, featuring a modern perspective on classic designs.

During the first quarter of fiscal 2018, we were negatively impacted by adverse weather affecting sales, manufacturing and delivery of our products. Additionally, our net sales and profitability were negatively affected by first run production for both the GSA business and floor samples for our new Passport collection. The GSA is now one of our ten largest customers. The high order volume from the GSA business with contractually short lead-times, together with the new product production runs further impacted production capacity which resulted in production and shipping delays to our retail customers that continued into the third quarter of fiscal 2018.

Beginning in March and continuing through the fourth quarter, we launched a major brand-building marketing program utilizing national television. This program targeted a broad demographic base beyond our core customer and we expect that as we continue to market to this broader base, our brand awareness will increase and ultimately drive increased revenues over time.

Gross margin was below the prior year primarily due to increased raw material costs, and a decrease in the retail sales mix in relation to total sales. This was partly offset by an inventory write-down of \$6.4 million during the third quarter of fiscal 2017, and a 4.9% increase in wholesale sales. Operating expenses increased slightly as a percentage of sales, mostly due to an increase in advertising expenses. Income taxes were reduced due to the U.S. Tax Cuts and Jobs Act changes enacted in December 2017. The net result was an increase in earnings per diluted share of \$0.03.

Net cash provided by operating activities along with operating cash and letters of credit under our credit facility enabled us to repurchase \$22.0 million of our common stock under our share repurchase program, pay off the remaining \$13.8 million of our term loan earlier than scheduled, and return \$29.5 million in cash dividends to our shareholders. At June 30, 2018 we had total cash and securities of \$22.4 million, and working capital of \$93.2 million.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

The components of consolidated revenues and operating income (loss) by business segment are as follows (in millions):

|                                         | Fiscal Year Ended June 30, |         |         |
|-----------------------------------------|----------------------------|---------|---------|
|                                         | 2018                       | 2017    | 2016    |
| <b>Revenue:</b>                         |                            |         |         |
| Wholesale segment                       | \$475.7                    | \$453.3 | \$491.5 |
| Retail segment                          | 587.5                      | 603.7   | 626.5   |
| Elimination of inter-segment sales      | (296.4)                    | (293.6) | (323.8) |
| Consolidated revenue                    | \$766.8                    | \$763.4 | \$794.2 |
| <b>Operating income (loss):</b>         |                            |         |         |
| Wholesale segment                       | \$48.5                     | \$53.5  | \$74.4  |
| Retail segment                          | (1.7 )                     | 1.2     | 16.5    |
| Adjustment for inter-company profit (1) | 2.1                        | 3.3     | (1.7 )  |
| Consolidated operating income           | \$48.9                     | \$58.0  | \$89.2  |

(1) Represents the change in wholesale profit contained in Ethan Allen operated design center inventory existing at the end of the period.

A summary by business segment of annual percentage changes from the preceding fiscal years are presented in the following tables:

|                          | Fiscal year ended June 30, |          |          |
|--------------------------|----------------------------|----------|----------|
|                          | 2018                       | 2017     | 2016     |
| <b>Wholesale segment</b> |                            |          |          |
| Revenue                  | 4.9 %                      | (7.8 %)  | 4.7 %    |
| Operating Income         | (9.4 %)                    | (28.1 %) | 11.1 %   |
| Backlog                  | 19.3 %                     | 17.6 %   | (36.8 %) |

|                                  | Fiscal year ended June 30, |         |       |
|----------------------------------|----------------------------|---------|-------|
|                                  | 2018                       | 2017    | 2016  |
| <b>Retail segment</b>            |                            |         |       |
| Revenue                          | (2.7 %)                    | (3.6 %) | 8.1 % |
| Comparable design center revenue | (3.2 %)                    | (4.6 %) | 8.3 % |
| Total written orders             | (3.1 %)                    | (0.9 %) | 1.7 % |

|                                         |           |          |          |
|-----------------------------------------|-----------|----------|----------|
| Comparable design center written orders | (3.8 %)   | (2.5 %)  | 1.8 %    |
| Operating Income                        | (245.1 %) | (92.7 %) | 853.1 %  |
| Backlog                                 | (2.3 %)   | (1.0 %)  | (13.1 %) |

## Business Results:

Our revenues are composed of (i) wholesale sales to independently operated and Company operated retail design centers and (ii) retail sales of Company operated design centers. See Note 15 to our Consolidated Financial Statements for the year ended June 30, 2018 included under Item 8 of this Annual Report.

### *Fiscal 2018 Compared to Fiscal 2017*

**Consolidated revenue** was \$766.8 million compared to \$763.4 million. There was a year-over-year increase in the wholesale segment and a decrease in the retail segment. Wholesale sales increased progressively throughout fiscal 2018 as the Company worked through production difficulties associated with the GSA contract business and first production runs discussed previously. This had a negative impact on retail segment sales through the first three quarters of fiscal 2018. Net sales for the fourth quarter of fiscal 2018 increased 11.4% and 1.9% for wholesale and retail respectively.

**Wholesale revenue** increased by \$22.4 million, or 4.9%, to \$475.7 million from \$453.3 million. The year-over-year increase was primarily attributable to higher sales from the GSA contract and our international independent design centers. There were 296 design centers globally as of June 30, 2018, a decrease of seven. Our international net sales to independent retailers was 7.0% of our consolidated net sales compared to 6.5%.

**Retail revenue** from Ethan Allen operated design centers decreased by \$16.2 million, or 2.7%, to \$587.5 million from \$603.7 million. Comparable store revenue decreased 3.2%. Year-over-year, written orders for the Company operated design centers decreased 3.1% and comparable design centers written orders decreased 3.8%. The reduction in sales is primarily a reflection of delayed shipments to the retail segment from the wholesale segment due to the timing of wholesale shipments previously mentioned.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

**Gross profit** decreased to \$416.0 million from \$419.7 million. The \$3.8 million decrease in gross profit was attributable to a \$16.2 million decrease in our retail segment sales, a lower mix of retail net sales to consolidated net sales of 76.6% compared to the 79.1% in the prior fiscal year, and increased raw material costs of \$4.7 million. These were partly offset by a fiscal 2017 write-down of inventory of \$6.4 million, and a current fiscal year increase in wholesale net sales of \$22.4 million.

**Operating expenses** increased \$5.3 million or 1.5% to \$367.1 million or 47.9% of net sales in fiscal 2018 from \$361.8 million or 47.4% of net sales in fiscal 2017. The increase in fiscal year 2018 expenses in absolute dollars and as a percent of net sales is primarily due to increased advertising costs of \$3.6 million.

**Operating income** for the fiscal year ended June 30, 2018 totaled \$48.9 million, or 6.4% of net sales, compared to \$58.0 million, or 7.6% of net sales, in the prior fiscal year. **Wholesale operating income** for fiscal 2018 totaled \$48.5 million, or 10.2% of net sales, as compared to \$53.5 million, or 11.8% of net sales, in the prior year. **Retail operating loss** was \$1.7 million, or -0.3% of sales, for fiscal 2018, compared to income of \$1.2 million, or 0.2% of sales, for fiscal 2017, a decrease of \$2.9 million. The decrease in consolidated operating income was primarily attributable to increased costs of raw materials, higher advertising costs due to national television advertising in the fiscal third and fourth quarters, reduced retail sales, as well as the disruptions caused by the first production runs of the GSA contract product and new product introductions.

**Interest and other related financing costs** decreased \$0.9 million to \$0.3 million from \$1.2 million in the prior fiscal year. The decrease is primarily due to lower interest expense throughout fiscal 2018 due to paying off our term loan in the first quarter of the current fiscal year and during late fiscal 2017 paying down \$25.0 million on our revolving credit facility to reduce our future debt carrying costs.

**Income tax expense** was \$12.7 million for fiscal 2018 and \$20.8 million for fiscal 2017. Our effective tax rate for fiscal 2018 was 25.9% compared to 36.5% in fiscal 2017. The effective tax rate for fiscal year 2018 primarily includes tax expense on the fiscal year's net income, the tax benefit lost on the cancelation of stock options, and also includes tax and interest expense on uncertain tax positions, partially offset by tax benefit from the re-measurement of deferred tax assets and liabilities and the vesting of restricted stock units. The effective tax rate for fiscal year 2017 primarily includes tax expense on that fiscal year's net income, and tax and interest expense on uncertain tax positions, partially offset by the reversal and recognition of some uncertain tax positions.

**Net income** for fiscal 2018 was \$36.4 million as compared to \$36.2 million in fiscal 2017. Net income per diluted share totaled \$1.32 in fiscal 2018 compared to \$1.29 per diluted share in the prior fiscal year.

*Fiscal 2017 Compared to Fiscal 2016*

**Consolidated revenue** was \$763.4 million compared to \$794.2 million. There was a year-over-year decline in sales in both the wholesale and retail segments.

**Wholesale revenue** decreased by \$38.1 million, or 7.8%, to \$453.3 million from \$491.5 million. The year-over-year decrease was attributable to lower sales to our Company operated design centers and domestic independent retailers, partly offset by an increase to our international independent design centers, primarily in China. There were 303 design centers globally as of June 30, 2017, an increase of seven. There was a net increase of two independently operated retail network locations, which included a decrease of one legacy location in the U.S. and the purchase of one independently owned location by the Company, bringing the total U.S. independent total to 48, and a net decrease of one location in China, bringing the China total to 82. Other international dealers opened five new locations. Our international net sales to independent retailers was 6.5% of our consolidated net sales compared to 5.4%.

**Retail revenue** from Ethan Allen operated design centers decreased by \$22.8 million, or 3.6%, to \$603.7 million from \$626.5 million. Comparable store revenue decreased 4.6%. Year-over-year, written orders for the Company operated design centers decreased 0.6% and comparable design centers written orders decreased 2.5%. Consumer spending patterns were disrupted during the fiscal year, especially around the election cycle, and negatively impacted sales.

**Gross profit** decreased to \$419.7 million from \$442.2 million. The \$22.5 million decrease in gross profit was attributable to decreases in both our retail and wholesale segment net sales and a write-down of inventory of \$6.4 million in the third quarter of fiscal 2017. This was partly offset by a slightly higher mix of retail net sales to consolidated net sales of 79.1% compared to the 78.9% in the prior fiscal year, and a decrease in cost of goods sold due to the net release of intercompany profit previously held in ending inventory.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

**Operating expenses** increased \$8.7 million or 2.5% to \$361.8 million or 47.4% of net sales in fiscal 2017 from \$353.1 million or 44.5% of net sales in fiscal 2016. The increase in fiscal year 2017 expenses in absolute dollars and as a percent of net sales is primarily due to increased advertising costs, a loss on disposal of real estate in fiscal 2017 compared to a gain on real estate sales in the prior fiscal year, and an increase in retail occupancy expense associated with a net increase of five design centers, partly offset by a reduction in incentive compensation.

**Operating income** for the fiscal year ended June 30, 2017 totaled \$58.0 million, or 7.6% of net sales, compared to \$89.2 million, or 11.2% of net sales, in the prior fiscal year. **Wholesale operating income** for fiscal 2017 totaled \$53.5 million, or 11.8% of net sales, as compared to \$74.4 million, or 15.1% of net sales, in the prior year. **Retail operating income** was \$1.2 million, or 0.2% of sales, for fiscal 2017, compared to \$16.5 million, or 2.6% of sales, for fiscal 2016, a decrease of \$15.3 million. The decrease in consolidated operating income was primarily attributable to decreased net sales, an inventory write-down at both our wholesale and retail segments due to a decision to reduce clearance and discontinued inventory by donation, increased advertising expenses, the net impact of real estate dispositions, and an increase in retail occupancy expense, partly offset by the net release of intercompany profit previously held in ending inventory and a reduction in incentive compensation.

**Interest and other related financing costs** decreased \$0.4 million to \$1.2 million from \$1.6 million in the prior fiscal year. The decrease is primarily due to lower interest expense throughout fiscal 2017 due to debt repayments during fiscal 2017 including a \$25.0 million paydown on our revolving credit facility to reduce our future debt carrying costs.

**Income tax expense** was \$20.8 million for fiscal 2017 and \$31.3 million for fiscal 2016. Our effective tax rate for fiscal 2017 was 36.5% compared to 35.6% in fiscal 2016. The effective tax rate for both fiscal years primarily includes tax expense on that fiscal year's net income, and tax and interest expense on uncertain tax positions, partially offset by the reversal and recognition of some uncertain tax positions.

**Net income** for fiscal 2017 was \$36.2 million as compared to \$56.6 million in fiscal 2016. Net income per diluted share totaled \$1.29 in fiscal 2017 compared to \$2.00 per diluted share in the prior fiscal year.

### Liquidity and Capital Resources

At June 30, 2018, we held unrestricted cash and equivalents of \$22.4 million and no restricted cash and investments. At June 30, 2017, we held unrestricted cash and cash equivalents of \$57.7 million and restricted cash and investments



of \$7.3 million. During fiscal 2018 we used cash to further pay down a portion of our debt and for common share repurchases. Our principal sources of liquidity include cash and cash equivalents, marketable securities, cash flow from operations, amounts available under our credit facility, and other borrowings.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

Under an agreement with the Company's private label consumer credit card provider (the "Lender"), at the end of each fiscal quarter we are required to maintain a minimum level of working capital. Due to market opportunities during the fourth quarter of fiscal 2018, the Company used \$22 million of its working capital to repurchase shares under our share repurchase program. This caused working capital to fall below this minimum at June 30, 2018, creating a Level 1 Collateral Event as defined in our agreement with the Lender. At any time during any Collateral Period, the Lender may require the Company to deliver within fifteen days of Lender's written request, either an Eligible Letter of Credit or Substitute Collateral. The Lender has not exercised this right but retains the ability to do so.

For a detailed discussion of our debt obligations and timing of our related cash payments see Note 6 to the Consolidated Financial Statements included under Item 8 of this Annual Report. A summary of net cash provided by (used in) operating, investing, and financing activities for each of the last three fiscal years is provided below (in millions):

|                                                           | Fiscal Years Ended<br>June 30, |          |          |
|-----------------------------------------------------------|--------------------------------|----------|----------|
|                                                           | 2018                           | 2017     | 2016     |
| <u>Cash provided by (used in) operating activities</u>    |                                |          |          |
| Net income plus depreciation and amortization             | \$56.2                         | \$56.3   | \$76.0   |
| Working capital items                                     | (13.0)                         | 14.5     | (19.3)   |
| Other operating activities                                | (0.7)                          | 7.8      | 1.7      |
| Total provided by operating activities                    | \$42.5                         | \$78.6   | \$58.4   |
| <u>Cash provided by (used in) investing activities</u>    |                                |          |          |
| Capital expenditures & acquisitions                       | \$(18.8)                       | \$(18.3) | \$(23.1) |
| Net sales of marketable securities                        | -                              | -        | 2.2      |
| Other investing activities                                | 7.9                            | 1.9      | 8.4      |
| Total used in investing activities                        | \$(10.9)                       | \$(16.4) | \$(12.5) |
| <u>Cash provided by (used in) financing activities</u>    |                                |          |          |
| Payments of long-term debt and capital lease obligations  | \$(14.5)                       | \$(28.4) | \$(34.8) |
| Borrowings from revolving credit and term loan facilities | \$-                            | \$-      | \$-      |
| Purchases and retirements of company stock                | (23.1)                         | (10.2)   | (19.3)   |
| Payment of cash dividends                                 | (29.5)                         | (20.0)   | (16.6)   |
| Other financing activities                                | 0.2                            | 1.3      | 1.6      |
| Total used in financing activities                        | \$(66.9)                       | \$(57.3) | \$(69.1) |

***Cash Provided By (Used in) Operating Activities***

In fiscal 2018 cash of \$42.5 million was provided by operating activities, a decrease of \$36.1 million from \$78.6 million in the prior year comparable period. Working capital items were a \$13.0 million use of cash in the current year and a \$14.5 million source of cash in the prior year, with a net difference of \$27.5 million. Most of the working capital difference was due to an inventory increase of \$11.9 million in the current year compared to a \$13.5 million source of cash in the prior year. Much of the prior year inventory decrease was due to a \$6.4 million write-down of inventory discussed previously in Business Results. Net income plus depreciation and amortization decreased \$0.1 million. Working capital items consist of current assets (accounts receivable, inventories, prepaid and other current assets) less current liabilities (customer deposits, payables, and accrued expenses and other current liabilities).

***Cash Provided By (Used in) Investing Activities***

In fiscal 2018, cash of \$10.9 million was used in investing activities, a decrease in cash used of \$5.5 million from \$16.4 million which was used during the prior year comparable period. This was due primarily to \$7.3 million of previously restricted cash being released and moved into the Company's operating accounts in exchange for a letter of credit. This was offset by less proceeds from the sale of real estate in fiscal 2018 than in the prior fiscal year. We anticipate that cash from operations will be sufficient to fund future capital expenditures in the near and longer term.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES*****Cash Provided By (Used in) Financing Activities***

In fiscal 2018, \$66.9 million was used in financing activities, a decrease of \$9.6 million from \$57.3 million in the prior year comparable period. During fiscal 2018 we paid \$13.8 million to pay off our term loan and utilized \$22.0 million to repurchase 950,484 shares at a weighted average cost of \$23.17 per share. At June 30, 2018 we have remaining Board authorization to repurchase 2.5 million shares. During fiscal 2018 we paid dividends of \$29.5 million, including a special dividend, an increase of 47.3% from the prior year. Cash dividends have been paid every quarter since July 1996. The following chart shows our dividend history by payment date from July 2013 to the present.

We expect to continue to declare regular quarterly dividends for the foreseeable future, business conditions permitting.

The following table summarizes, as of June 30, 2018, the timing of cash payments related to our outstanding contractual obligations (in millions):

|                               | Total   | Less<br>than<br>1<br>Year | 1-3<br>Years | 4-5<br>Years | More<br>than<br>5<br>Years |
|-------------------------------|---------|---------------------------|--------------|--------------|----------------------------|
| Long-term debt obligations:   |         |                           |              |              |                            |
| Debt maturities               | \$1.7   | \$0.6                     | \$1.0        | \$0.1        | \$-                        |
| Contractual interest          | 0.1     | 0.1                       | 0.1          | -            | -                          |
| Operating lease obligations   | 176.0   | 34.4                      | 55.4         | 39.2         | 47.0                       |
| Letters of credit             | 6.2     | 6.2                       | -            | -            | -                          |
| Purchase obligations (1)      | -       | -                         | -            | -            | -                          |
| Other long-term liabilities   | 0.2     | -                         | -            | -            | 0.2                        |
| Total contractual obligations | \$184.2 | \$41.3                    | \$56.4       | \$39.3       | \$47.2                     |

(1) For purposes of this table, purchase obligations are defined as agreements that are enforceable and legally binding and that specify all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. While we are not a party to any significant

long-term supply contracts or purchase commitments, we do, in the normal course of business, regularly initiate purchase orders for the procurement of (i) selected finished goods sourced from third-party suppliers, (ii) lumber, fabric, leather and other raw materials used in production, and (iii) certain outsourced services. All purchase orders are based on current needs and are fulfilled by suppliers within short time periods. At June 30, 2018, our open purchase orders with respect to such goods and services totaled approximately \$40 million.

Further discussion of our contractual obligations associated with outstanding debt and lease arrangements can be found in Notes 6 and 7, respectively, to the Consolidated Financial Statements included under Item 8 of this Annual Report.

We believe that our cash flow from operations, together with our other available sources of liquidity, will be adequate to make all required payments of principal and interest on our debt, to permit anticipated capital expenditures, and to fund working capital and other cash requirements. As of June 30, 2018, we had working capital of \$93.2 million compared to \$116.7 million at June 30, 2017, a decrease of \$23.5 million and a current ratio of 1.77 to 1 at June 30, 2018 and 1.92 to 1 at June 30, 2017. In addition to using available cash to fund changes in working capital, necessary capital expenditures, acquisition activity, the repayment of debt, and the payment of dividends, the Company has been authorized by our board of directors to repurchase our common stock, from time to time, either directly or through agents, in the open market at prices and on terms satisfactory to us.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **Off-Balance Sheet Arrangements and Other Commitments, Contingencies and Contractual Obligations**

Except as indicated below, we do not utilize or employ any off-balance sheet arrangements, including special-purpose entities, in operating our business. As such, we do not maintain any (i) retained or contingent interests, (ii) derivative instruments, or (iii) variable interests which could serve as a source of potential risk to our future liquidity, capital resources and results of operations.

We may, from time to time in the ordinary course of business, provide guarantees on behalf of selected affiliated entities or become contractually obligated to perform in accordance with the terms and conditions of certain business agreements. The nature and extent of these guarantees and obligations may vary based on our underlying relationship with the benefiting party and the business purpose for which the guarantee or obligation is being provided. The only such program in place at both June 30, 2018 and June 30, 2017 was for our consumer credit program described below.

#### ***Ethan Allen Consumer Credit Program***

The terms and conditions of our consumer credit program, which is financed and administered by a third-party financial institution on a non-recourse basis to Ethan Allen, are set forth in an agreement between the Company and that financial service provider (the “Program Agreement”) which was last amended effective January 2014. Any independent retailer choosing to participate in the consumer credit program is required to enter into a separate agreement with that same third-party financial institution which sets forth the terms and conditions under which the retailer is to perform in connection with its offering of consumer credit to its customers (the “Retailer Agreement”). We have obligated ourselves on behalf of any independent retailer choosing to participate in our consumer credit program by agreeing, in the event of default, breach, or failure of the independent retailer to perform under such Retailer Agreement, to take on certain responsibilities of the independent retailer, including, but not limited to, delivery of goods and reimbursement of customer deposits. Customer receivables originated by independent retailers remain non-recourse to Ethan Allen. The Program Agreement will terminate on July 31, 2019, but includes a provision for automatic one-year renewals unless either party gives notice of termination. While the maximum potential amount of future payments (undiscounted) that we could be required to make under this obligation is indeterminable, recourse provisions exist that would enable us to recover, from the independent retailer, any amount paid or incurred by us related to our performance. Based on the underlying creditworthiness of our independent retailers, including their historical ability to perform satisfactorily in connection with the terms of our consumer credit program, we believe this obligation will expire without requiring funding by us. To ensure funding for delivery of products sold, the terms of the Program Agreement also contain a right for the financial services provider to demand from the Company collateral at a variable rate based on the volume of program sales if the Company does not meet certain covenants, including a minimum working capital requirement. At June 30 of 2018, we were below this minimum capital requirement, defined in the agreement as a Level 1 Collateral Event. At any time the lender may require the Company

to deliver within fifteen days of lenders request, either an Eligible Letter of Credit, or Substitute Collateral for approximately \$4 million. The lender has not made a demand for collateral as of the date of this Annual Report on Form 10-K, but if they were to do so, we have adequate borrowing capacity under our Facility to satisfy this demand.

### ***Product Warranties***

Our products, including our case goods, upholstery and home accents, generally carry explicit product warranties that extend up to seven years and are provided based on terms that are generally accepted in the industry. All our domestic independent retailers are required to enter into, and perform in accordance with the terms and conditions of, a warranty service agreement. We record provisions for estimated warranty and other related costs at time of sale based on historical warranty loss experience and make periodic adjustments to those provisions to reflect actual experience. On rare occasion, certain warranty and other related claims involve matters of dispute that ultimately are resolved by negotiation, arbitration or litigation. In certain cases, a material warranty issue may arise which is beyond the scope of our historical experience. We provide for such warranty issues as they become known and are deemed to be both probable and estimable. It is reasonably possible that, from time to time, additional warranty and other related claims could arise from disputes or other matters beyond the scope of our historical experience. As of June 30, 2018 and 2017, the Company's product warranty liability totaled \$1.5 million and \$1.3 million, respectively.

### **Impact of Inflation**

We believe inflation had an impact on our business the last three fiscal years but we have generally been able to create operational efficiencies, seek lower cost alternatives, or raise selling prices to offset increases in product and operating costs. It is possible in the future that we will not be successful in our efforts to offset the impacts from inflation.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

### **Business Outlook**

We continue to strengthen our vertically integrated structure from concept of idea, to engineering, to manufacturing, to retail and logistics. We intend to maintain strong manufacturing capabilities in North America, which we believe is a long-term competitive advantage that will allow us to advance our objectives of maintaining fast order delivery, exceptional quality and improving capacity to ship stocked and custom made-to-order items more quickly, which in turn will allow us to grow our business. In December 2017, the Tax Act substantially reduced our effective tax rate. We expect our effective tax rate to be approximately 24% to 25% for fiscal 2019.

Our network of professionally trained interior design professionals differentiates us significantly from our competitors. We continue to strengthen the level of service, professionalism, and interior design competence, as well as to improve the efficiency of our retail operations. We believe that over time, we will continue to benefit from (i) continuous repositioning of our retail network, (ii) frequent new product introductions, (iii) new and innovative marketing promotions and effective use of targeted advertising media, and (iv) continued use of the latest technology combined with personal service from our interior design professionals.

We have completed a major transformation of our product offerings, which refreshed over 70% of our entire line of products. During the third quarter of fiscal 2017 we expanded the reach of our Ethan Allen | Disney product program by selling a curated selection on Disneystore.com, we expanded our contract sales with the GSA and other contract customers and entered into an agreement with Amazon to sell products through the Amazon marketplace. Now that we have completed this major transformation, we believe that we are well positioned to leverage all the actions we have taken.

We expect the home furnishings industry to remain extremely competitive with respect to both the sourcing of products and the wholesale and retail sale of those products for the foreseeable future. Domestic manufacturers continue to face pricing pressures because of the lower manufacturing costs on imports, particularly from Asia. While we also utilize overseas sourcing for approximately one quarter of our products, we choose to differentiate ourselves by maintaining a substantial North American manufacturing base, the majority of which is located in the United States. This structure enables us to leverage our vertically integrated structure to our advantage. We continue to believe that a balanced approach to product sourcing, which includes our own North American manufacturing of about 75% of our product offerings coupled with the import of other selected products, provides the greatest degree of flexibility and shorter lead times and is the most effective approach to ensuring that acceptable levels of quality, service and value are attained.



We therefore remain cautiously optimistic about our performance due to the many strong programs already in place and others we currently plan to introduce in the coming months. Our retail strategy involves (i) a continued focus on providing relevant product offerings, a wide array of product solutions, and superior interior design solutions through our large staff of interior design professionals, (ii) continuing strong advertising and marketing campaigns to get our message across and to continue broadening our customer base, (iii) the opening of new or relocated design centers in more prominent locations, and encouraging independent retailers to do the same, (iv) leveraging the use of technology and personal service within our retail network and online through [www.ethanallen.com](http://www.ethanallen.com), and (v) further expansion internationally. We believe this strategy provides an opportunity to grow our business. Further discussion of the home furnishings industry has been included under Item 1 of this Annual Report.

### **Recent Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued ASU 2014-09, *Revenue from Contracts with Customers*. This ASU provides a framework for revenue recognition that replaces most existing GAAP revenue recognition guidance when it becomes effective. The core principle of the ASU is that a company will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard also requires expanded disclosures about the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. We will adopt the new standard effective July 1, 2018, and plan on using the modified retrospective approach and will record the cumulative effect of applying this standard to opening retained earnings. We have substantially completed a comprehensive review of our revenue streams and contracts as they relate to this guidance and based on the work performed to date, we do not expect that the adoption will have a material impact on the amount or timing of revenue recognized on an ongoing basis. Upon adoption we will recognize an asset related to product returns and a corresponding liability for estimated returns and allowances.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

In February 2016, the FASB issued ASU 2016-02, *Leases*. This guidance requires an entity to recognize lease liabilities and a right-of-use asset for all leases on the balance sheet and to disclose key information about the entity's leasing arrangements. ASU 2016-02 is effective for the Company on July 1, 2019, and early adoption is permitted. ASU 2016-02 is required to be adopted using a modified retrospective approach for all leases existing at, or entered into after the date of initial adoption, with an option to elect to use certain transition relief. The Company is currently evaluating the impact of this new standard on its consolidated financial statements and related disclosures, but expects that it will result in a significant increase in the assets and liabilities recorded on the consolidated balance sheet upon adoption.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): *Restricted Cash*. It is intended to reduce diversity in the presentation of restricted cash and restricted cash equivalents in the statement. The statement requires that restricted cash and restricted cash equivalents be included as components of total cash and cash equivalents as presented on the statement of cash flows. The Company currently does not include restricted cash as a component of cash and equivalents as presented on the statement of cash flows. The new guidance is effective for the Company on July 1, 2018, with early adoption permitted. The Company is currently evaluating the impact on our consolidated financial statements. We plan on adopting effective July 1, 2018.

### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to market risks relating to fluctuations in interest rates and foreign currency exchange rates.

Interest rate risk exists primarily through our borrowing activities. We utilize United States dollar denominated borrowings to fund substantially all our working capital and investment needs. Short-term debt, if required, is used to meet working capital requirements and long-term debt is generally used to finance long-term investments. There is inherent rollover risk for borrowings as they mature and are renewed at current market rates. The extent of this risk is not quantifiable or predictable because of the variability of future interest rates and our future financing requirements.

For floating-rate obligations, interest rate changes do not affect the fair value of the underlying financial instrument but would impact future earnings and cash flows, assuming other factors are held constant. Conversely, for fixed-rate obligations, interest rate changes affect the fair value of the underlying financial instrument but would not impact earnings or cash flows. At June 30, 2018, we did not have any floating-rate debt obligations outstanding under our Facility. We currently do not engage in any interest rate hedging activity and we have no intention of doing so in the foreseeable future. Based on the average interest rate of the loans under the Facility during the quarter ended June 30, 2018, and to the extent that borrowings were outstanding, a 10% change in the interest rate would not have a material

effect on our consolidated results of operations and financial condition.

Foreign currency exchange risk is primarily limited to our operation of Ethan Allen operated retail design centers located in Canada and our plants in Mexico and Honduras, as substantially all purchases of imported parts and finished goods are denominated in United States dollars. As such, gains or losses resulting from market changes in the value of foreign currencies have not had, nor are they expected to have, a material effect on our consolidated results of operations. A decrease in the value of foreign currencies (in particular Asian) relative to the United States dollar may affect the profitability of our vendors but as we employ a balanced sourcing strategy, we believe any impact would be moderate relative to peers in the industry.

**Item 8. Financial Statements and Supplementary Data**

Our Consolidated Financial Statements and Supplementary Data are listed in Item 15 of this Annual Report.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **Report of Independent Registered Public Accounting Firm**

To the Shareholders and Board of Directors  
Ethan Allen Interiors Inc.:

#### *Opinions on the Consolidated Financial Statements and Internal Control Over Financial Reporting*

We have audited the accompanying consolidated balance sheets of Ethan Allen Interiors Inc. and subsidiaries (the “Company”) as of June 30, 2018 and 2017, the related consolidated statements of comprehensive income, shareholders’ equity, and cash flows for each of the years in the three-year period ended June 30, 2018, and the related notes (collectively, the “consolidated financial statements”). We also have audited the Company’s internal control over financial reporting as of June 30, 2018, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of June 30, 2018 and 2017, and the results of its operations and its cash flows for each of the years in the three-year period ended June 30, 2018, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of June 30, 2018, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

#### *Basis for Opinions*

The Company’s management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company’s consolidated financial statements and an opinion on the Company’s internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### *Definition and Limitations of Internal Control Over Financial Reporting*

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ KPMG LLP

We have served as the Company's auditor since 1989.

Stamford, Connecticut  
August 2, 2018

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

**Consolidated  
Balance  
Sheets  
June 30,  
2018 and  
2017  
(In  
thousands,  
except share  
data)**

|                                                                                                                                                        | 2018      | 2017      |
|--------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|-----------|
| <b>ASSETS</b>                                                                                                                                          |           |           |
| Current assets:                                                                                                                                        |           |           |
| Cash and cash equivalents                                                                                                                              | \$22,363  | \$57,701  |
| Accounts receivable, net                                                                                                                               | 12,364    | 12,293    |
| Inventories                                                                                                                                            | 163,012   | 149,483   |
| Prepaid expenses and other current assets                                                                                                              | 16,686    | 23,621    |
| Total current assets                                                                                                                                   | 214,425   | 243,098   |
| Property, plant and equipment, net                                                                                                                     | 267,903   | 270,198   |
| Goodwill and other intangible assets                                                                                                                   | 45,128    | 45,128    |
| Restricted cash and investments                                                                                                                        | -         | 7,330     |
| Other assets                                                                                                                                           | 2,977     | 2,468     |
| Total assets                                                                                                                                           | \$530,433 | \$568,222 |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                                                                                                            |           |           |
| Current liabilities:                                                                                                                                   |           |           |
| Current maturities of long-term debt                                                                                                                   | \$584     | \$2,731   |
| Customer deposits                                                                                                                                      | 61,248    | 62,960    |
| Accounts payable                                                                                                                                       | 18,768    | 16,961    |
| Accrued compensation and benefits                                                                                                                      | 18,926    | 20,352    |
| Accrued expenses and other current liabilities                                                                                                         | 21,734    | 23,441    |
| Total current liabilities                                                                                                                              | 121,260   | 126,445   |
| Long-term debt                                                                                                                                         | 1,096     | 11,608    |
| Other long-term liabilities                                                                                                                            | 24,207    | 29,273    |
| Total liabilities                                                                                                                                      | 146,563   | 167,326   |
| Shareholders' equity:                                                                                                                                  |           |           |
| Common stock, par value \$0.01; 150,000,000 shares authorized; 48,989,060 shares issued at June 30, 2018 and 48,979,994 shares issued at June 30, 2017 | 490       | 490       |
| Preferred stock, par value \$0.01; 1,055,000 shares authorized; none issued                                                                            | -         | -         |
| Additional paid-in-capital                                                                                                                             | 376,950   | 377,550   |
| Less: Treasury stock (at cost), 22,459,766 shares at June 30, 2018 and 21,532,779 shares at June 30, 2017                                              | (656,551) | (635,179) |

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|                                                       |           |           |
|-------------------------------------------------------|-----------|-----------|
| Retained earnings                                     | 669,013   | 661,976   |
| Accumulated other comprehensive income (loss)         | (6,171 )  | (4,131 )  |
| Total Ethan Allen Interiors Inc. shareholders' equity | 383,731   | 400,706   |
| Noncontrolling interests                              | 139       | 190       |
| Total shareholders' equity                            | 383,870   | 400,896   |
| Total liabilities and shareholders' equity            | \$530,433 | \$568,222 |

See accompanying notes to consolidated financial statements.



**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

**Consolidated Statements of Comprehensive Income**  
**For Years Ended June 30, 2018, 2017, and 2016**  
(In thousands, except share data)

|                                              | 2018      | 2017      | 2016      |
|----------------------------------------------|-----------|-----------|-----------|
| Net sales                                    | \$766,784 | \$763,385 | \$794,202 |
| Cost of sales                                | 350,820   | 343,662   | 351,966   |
| Gross profit                                 | 415,964   | 419,723   | 442,236   |
| Selling, general and administrative expenses | 367,097   | 361,773   | 353,057   |
| Operating income                             | 48,867    | 57,950    | 89,179    |
| Interest and other income (expense)          | 525       | 268       | 395       |
| Interest and other related financing costs   | 325       | 1,223     | 1,618     |
| Income before income taxes                   | 49,067    | 56,995    | 87,956    |
| Income tax expense                           | 12,696    | 20,801    | 31,319    |
| Net income                                   | \$36,371  | \$36,194  | \$56,637  |
| <u>Per share data:</u>                       |           |           |           |
| Net income per basic share                   | \$1.33    | \$1.31    | \$2.02    |
| Basic weighted average common shares         | 27,321    | 27,679    | 28,072    |
| Net income per diluted share                 | \$1.32    | \$1.29    | \$2.00    |
| Diluted weighted average common shares       | 27,625    | 27,958    | 28,324    |
| Dividends declared per common share          | \$1.07    | \$0.74    | \$0.62    |
| Comprehensive income:                        |           |           |           |
| Net income                                   | \$36,371  | \$36,194  | \$56,637  |
| Other comprehensive income                   |           |           |           |
| Currency translation adjustment              | (2,040 )  | 715       | (2,208 )  |
| Other                                        | (51 )     | (14 )     | 27        |
| Other comprehensive income (loss) net of tax | (2,091 )  | 701       | (2,181 )  |
| Comprehensive income                         | \$34,280  | \$36,895  | \$54,456  |

See accompanying notes to consolidated financial statements.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows**  
**For Years Ended June 30, 2018, 2017, and 2016**  
(In thousands)

|                                                                                    | 2018     | 2017     | 2016     |
|------------------------------------------------------------------------------------|----------|----------|----------|
| <b>Operating activities:</b>                                                       |          |          |          |
| Net income                                                                         | \$36,371 | \$36,194 | \$56,637 |
| Adjustments to reconcile net income to net cash provided by operating activities:  |          |          |          |
| Depreciation and amortization                                                      | 19,831   | 20,115   | 19,353   |
| Compensation expense related to share-based payment awards                         | 954      | 1,259    | 2,356    |
| Provision (benefit) for deferred income taxes                                      | (106 )   | 3,507    | 671      |
| Loss (gain) on disposal of property, plant and equipment                           | 201      | 1,033    | (2,267 ) |
| Other                                                                              | (250 )   | (6 )     | (1,295 ) |
| Change in operating assets and liabilities, net of effects of acquired businesses: |          |          |          |
| Accounts receivable                                                                | (682 )   | (2,826 ) | 2,926    |
| Inventories                                                                        | (11,876) | 13,507   | (9,982 ) |
| Prepaid and other current assets                                                   | 3,274    | 1,010    | 5,113    |
| Customer deposits                                                                  | (2,444 ) | 1,883    | (7,275 ) |
| Accounts payable                                                                   | 1,807    | 1,524    | (3,509 ) |
| Accrued expenses and other current liabilities                                     | (3,058 ) | (547 )   | (6,550 ) |
| Other assets and liabilities                                                       | (1,525 ) | 1,980    | 2,191    |
| Net cash provided by operating activities                                          | 42,497   | 78,633   | 58,369   |
| <b>Investing activities:</b>                                                       |          |          |          |
| Proceeds from the disposal of property, plant & equipment                          | 327      | 1,273    | 8,073    |
| Change in restricted cash and investments                                          | 7,330    | 490      | 190      |
| Capital expenditures and acquisitions                                              | (18,773) | (18,321) | (23,132) |
| Sales of marketable securities                                                     | -        | -        | 2,150    |
| Other investing activities                                                         | 204      | 175      | 193      |
| Net cash used in investing activities                                              | (10,912) | (16,383) | (12,526) |
| <b>Financing activities:</b>                                                       |          |          |          |
| Payments on long-term debt and capital lease obligations                           | (14,456) | (28,401) | (34,840) |
| Purchases and retirements of company stock                                         | (23,120) | (10,246) | (19,346) |
| Payment of cash dividends                                                          | (29,509) | (20,031) | (16,646) |
| Other financing activities                                                         | 194      | 1,335    | 1,718    |
| Net cash used in financing activities                                              | (66,891) | (57,343) | (69,114) |
| Effect of exchange rate changes on cash                                            | (32 )    | 135      | (252 )   |
| Net increase (decrease) in cash & cash equivalents                                 | (35,338) | 5,042    | (23,523) |
| Cash & cash equivalents - beginning of year                                        | 57,701   | 52,659   | 76,182   |
| Cash & cash equivalents - end of year                                              | \$22,363 | \$57,701 | \$52,659 |

Supplemental cash flow information:

|                                             |          |          |          |
|---------------------------------------------|----------|----------|----------|
| Income taxes paid                           | \$14,305 | \$15,074 | \$29,003 |
| Interest paid                               | \$177    | \$936    | \$1,352  |
| Non-cash capital lease obligations incurred | \$1,442  | \$613    | \$-      |

See accompanying notes to consolidated financial statements.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

**Consolidated Statements of Shareholders' Equity**  
**For Years Ended June 30, 2018, 2017, and 2016**  
(In thousands, except share data)

|                                                            | Common<br>Stock | Additional<br>Paid-in<br>Capital | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Income | Retained<br>Earnings | Non-<br>Controlling<br>Interests | Total     |
|------------------------------------------------------------|-----------------|----------------------------------|-------------------|-------------------------------------------------|----------------------|----------------------------------|-----------|
| Balance at June 30, 2015                                   | 489             | 370,914                          | (605,586)         | (2,638 )                                        | 607,079              | 277                              | 370,535   |
| Stock issued on share-based awards                         | -               | 734                              | -                 | -                                               | -                    | -                                | 734       |
| Compensation expense associated with share-based awards    | -               | 2,356                            | -                 | -                                               | -                    | -                                | 2,356     |
| Tax benefit associated with exercise of share based awards | -               | 968                              | -                 | -                                               | -                    | -                                | 968       |
| Purchase/retirement of company stock                       | -               | -                                | (19,346 )         | -                                               | -                    | -                                | (19,346 ) |
| Dividends declared on common stock                         | -               | -                                | -                 | -                                               | (17,401 )            | -                                | (17,401 ) |
| Capital distribution                                       | -               | -                                | -                 | -                                               | -                    | (100 )                           | (100 )    |
| Comprehensive income (loss)                                | -               | -                                | -                 | (2,208 )                                        | 56,637               | 27                               | 54,456    |
| Balance at June 30, 2016                                   | 489             | 374,972                          | (624,932)         | (4,846 )                                        | 646,315              | 204                              | 392,202   |
| Stock issued on share-based awards                         | 1               | 1,199                            | -                 | -                                               | -                    | -                                | 1,200     |
| Compensation expense associated with share-based awards    | -               | 1,259                            | -                 | -                                               | -                    | -                                | 1,259     |
| Tax benefit associated with exercise of share based awards | -               | 120                              | -                 | -                                               | -                    | -                                | 120       |
| Purchase/retirement of company stock                       | -               | -                                | (10,247 )         | -                                               | -                    | -                                | (10,247 ) |
| Dividends declared on common stock                         | -               | -                                | -                 | -                                               | (20,533 )            | -                                | (20,533 ) |
| Capital distribution                                       | -               | -                                | -                 | -                                               | -                    | -                                | -         |
| Comprehensive income (loss)                                | -               | -                                | -                 | 715                                             | 36,194               | (14 )                            | 36,895    |
| Balance at June 30, 2017                                   | 490             | 377,550                          | (635,179)         | (4,131 )                                        | 661,976              | 190                              | 400,896   |
| Stock issued on share-based awards                         | \$ -            | \$ 193                           | -                 | -                                               | -                    | \$ -                             | \$ 193    |
| Compensation expense associated with share-based awards    | -               | 954                              | -                 | -                                               | -                    | -                                | 954       |

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|                                                            |        |           |             |             |           |        |           |
|------------------------------------------------------------|--------|-----------|-------------|-------------|-----------|--------|-----------|
| Tax benefit associated with exercise of share based awards | -      | -         | -           | -           | -         | -      | -         |
| Purchase/retirement of company stock                       | -      | (1,747 )  | (21,372 )   | -           | -         | -      | (23,119 ) |
| Dividends declared on common stock                         | -      | -         | -           | -           | (29,334 ) | -      | (29,334 ) |
| Capital distribution                                       | -      | -         | -           | -           | -         | -      | -         |
| Comprehensive income (loss)                                | -      | -         | -           | (2,040 )    | 36,371    | (51 )  | 34,280    |
| Balance at June 30, 2018                                   | \$ 490 | \$376,950 | \$(656,551) | \$ (6,171 ) | \$669,013 | \$ 139 | \$383,870 |

See accompanying notes to consolidated financial statements.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements

June 30, 2018, 2017 and 2016

#### (I) Summary of Significant Accounting Policies

##### Basis of Presentation

The following is a summary of significant accounting policies of Ethan Allen Interiors Inc., and its wholly-owned subsidiaries (collectively "We," "Us," "Our," "Ethan Allen" or the "Company"). All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements. Our consolidated financial statements also include the accounts of an entity in which we are a majority shareholder with the power to direct the activities that most significantly impact the entity's performance. Noncontrolling interest amounts in the entity are immaterial and included in the Consolidated Statement of Comprehensive Income within interest and other income, net.

##### Nature of Operations

We are a leading manufacturer and retailer of quality home furnishings and accents, offering complimentary interior design service to our clients and sell a full range of furniture products and decorative accents. We sell our products through *one* of the country's largest home furnishing retail networks and at *June 30, 2018* there were a total of 296 design centers in our retail network, of which 148 are Company operated and 148 are independently operated. Nearly all our Company operated retail design centers are located in the United States, with the remaining Company operated design centers located in Canada. The majority of the independently operated design centers are in Asia, with the remaining independently operated design centers located throughout the United States, the Middle East and Europe. We own and operate *nine* manufacturing facilities including *six* manufacturing plants and *one* sawmill in the United States and *one* manufacturing plant in Mexico and *one* in Honduras.

##### Use of Estimates

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States, which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Because of the inherent uncertainty involved in making those estimates, actual results could differ from those estimates. Areas in which significant estimates have been made include, but are *not* limited to, revenue recognition, the allowance for doubtful accounts receivable, inventory obsolescence, tax valuation allowances, useful lives and impairment analyses for property, plant and equipment and definite lived intangible assets, goodwill and indefinite lived intangible asset impairment analyses, the evaluation of uncertain tax positions and the fair value of assets acquired and liabilities assumed in business combinations.

### Reclassifications

Certain reclassifications have been made to prior years' financial statements to conform to the current year's presentation. These changes were made for disclosure purposes only and did *not* have any impact on previously reported results.

### Cash and Cash Equivalents

Cash and short-term, highly liquid investments with original maturities of *three* months or less are considered cash and cash equivalents. We invest excess cash in money market accounts, short-term commercial paper, and U.S. Treasury Bills.

### Inventories

Inventories are stated at the lower of cost (*first-in, first-out*) and net realizable value. Cost is determined based solely on those charges incurred in the acquisition and production of the related inventory (i.e. material, labor and manufacturing overhead costs).

### Property, Plant and Equipment

Property, plant and equipment are stated at cost, net of accumulated depreciation and amortization. Depreciation of property, plant and equipment is provided over the estimated useful lives of the respective assets on a straight-line basis. Estimated useful lives of the respective assets typically range from *twenty* to *forty* years for buildings and improvements and from *three* to *twenty* years for machinery and equipment. Leasehold improvements are amortized

over the shorter of the underlying lease term or the estimated useful life.



## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

### Operating Leases

We record expense for operating leases on a straight-line basis, beginning on the date that we take possession or control of the property. Several of our operating lease agreements contain provisions for tenant improvement allowances, rent holidays, rent concessions, and/or rent escalations.

Incentive payments received from landlords are recorded as deferred lease incentives and are amortized over the underlying lease term on a straight-line basis as a reduction of rent expense. When the terms of an operating lease provide for periods of free rent, rent concessions, and/or rent escalations, we establish a deferred rent liability for the difference between the scheduled rent payment and the straight-line rent expense recognized. This deferred rent liability is also amortized over the underlying lease term on a straight-line basis as a reduction of rent expense.

### Goodwill and Other Intangible Assets

Our intangible assets are comprised primarily of goodwill, which represents the excess of cost over the fair value of net assets acquired, and trademarks. We determined these assets have indefinite useful lives, and are therefore *not* amortized.

### Impairment of Long-Lived Assets and Goodwill

Goodwill and other indefinite-lived intangible assets are evaluated for impairment on an annual basis during the *fourth* quarter of each fiscal year, and between annual tests whenever events or circumstances indicate that the carrying value of the goodwill or other intangible asset *may* exceed its fair value. When testing goodwill for impairment, we *may* assess qualitative factors for some or all of our reporting units to determine whether it is more likely than *not* (that is, a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount, including goodwill. Alternatively, we *may* bypass this qualitative assessment for some or all of our reporting units and determine whether the carrying value exceeds the fair value using a quantitative assessment, as described below.

The recoverability of long-lived assets is evaluated for impairment whenever events or changes in circumstances indicate that we *may not* be able to recover the carrying amount of an asset or asset group. Our assessment of

recoverability determines whether the carrying value will be recovered through the expected undiscounted future cash flows resulting from the use of the asset. In the event the sum of the expected undiscounted future cash flows is less than the carrying value of the asset, an impairment loss equal to the excess of the asset's carrying value over its fair value is recorded.

The fair value of our trade name, which is the Company's only indefinite-lived intangible asset other than goodwill, is valued using the relief-from-royalty method. Significant factors used in trade name valuation are rates for royalties, future growth, and a discount factor. Royalty rates are determined using an average of recent comparable values. Future growth rates are based on the Company's perception of the long-term values in the market in which we compete, and the discount rate is determined using the weighted average cost of capital for companies within our peer group, adjusted for specific company risk premium factors.

### Financial Instruments

Because of their short-term nature, the carrying value of our cash and cash equivalents, receivables and payables, short-term debt and customer deposit liabilities approximates fair value. At June 30, 2018 our debt consists entirely of capital leases, and at June 30, 2017 it consisted of our term loan and capital leases. The estimated fair value is equal to the carrying value on those dates.

### Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards.

Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance must be established for deferred tax assets when it is more likely than *not* that the assets will *not* be realized.

We recognize the tax benefit from an uncertain tax position only if it is more likely than *not* that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. Most of the unrecognized tax benefits, if recognized, would be recorded as a benefit to income tax expense.



## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

The liability associated with an unrecognized tax benefit is classified as a long-term liability except for the amount for which a cash payment is expected to be made or tax positions settled within *one* year. We recognize interest and penalties related to income tax matters as a component of income tax expense.

### Revenue Recognition

Revenue is recognized when all the following have occurred: persuasive evidence of a sales arrangement exists (e.g. a wholesale purchase order or retail sales order); the sales arrangement specifies a fixed or determinable sales price; title and risk of ownership has passed to the customer; *no* specific performance obligations remain; product is shipped or services are provided to the customer; collectability is reasonably assured. As such, revenue recognition generally occurs upon the shipment of goods to independent retailers or, in the case of Ethan Allen operated retail design centers, upon delivery to the customer. If shipping is billed to customers, this is included in revenue. Recorded sales provide for estimated returns and allowances. We permit our customers to return defective products and incorrect shipments, and terms we offer are standard for the industry.

### Shipping and Handling Costs

Our practice has been to sell our products at the same delivered cost to all retailers nationwide, regardless of shipping point. Costs incurred by the Company to deliver finished goods are expensed and recorded in selling, general and administrative expenses. Shipping and handling costs amounted to \$73.6 million in fiscal year 2018, \$71.3 million for fiscal 2017 and \$71.7 million in fiscal 2016.

### Advertising Costs

Advertising costs are expensed when *first* aired or distributed. Our total advertising costs were \$43.3 million in fiscal year 2018, \$39.7 million in fiscal year 2017 and \$34.1 million in fiscal year 2016. These amounts include advertising media expenses, outside and inside agency expenses, certain website related fees and photo and video production. Prepaid advertising costs at *June 30, 2018* totaled \$1.1 million compared to \$1.5 million at *June 30, 2017*.

### Earnings Per Share

We compute basic earnings per share by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated similarly, except that the weighted average outstanding shares are adjusted to include the effects of converting all potentially dilutive share-based awards issued under our employee stock plans (see Notes 9 and 10).

### Share-Based Compensation

We estimate, as of the date of grant, the fair value of stock options awarded using the Black-Scholes option pricing model. Use of a valuation model requires management to make certain assumptions with respect to selected model inputs, including anticipated changes in the underlying stock price (i.e. expected volatility) and option exercise activity (i.e. expected life). Expected volatility is based on the historical volatility of our stock and other contributing factors. The expected life of options granted, which represents the period of time that the options are expected to be outstanding, is based, primarily, on historical data. We estimate, as of the date of grant, the fair value of restricted stock units awarded using a discounted cash flow model which requires management to make certain assumptions with respect to model inputs including anticipated future dividends *not* paid during the restriction period, and a discount for lack of marketability for a *one*-year holding period after vesting.

Share-based compensation expense is included within selling, general and administrative expenses. Tax benefits associated with our share-based compensation arrangements are included within income tax expense.

All shares of our common stock received in connection with the exercise of share-based awards have been recorded as treasury stock and result in a reduction in shareholders' equity.

### Foreign Currency Translation

The functional currency of each Company operated foreign location is the respective local currency. Assets and liabilities are translated into United States dollars using the current period-end exchange rate and income and expense amounts are translated using the average exchange rate for the period in which the transaction occurred. Resulting translation adjustments are reported as a component of accumulated other comprehensive income within shareholders' equity.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

### Recently Adopted Accounting Pronouncements

In *July 2015*, the FASB issued ASU 2015-11, “*Inventory (Topic 330): Simplifying the Measurement of Inventory*,” which states that inventory should be measured at the lower of cost and net realizable value. Net realizable value is defined as estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. We adopted effective *July 1, 2017*, and the new guidance is being applied prospectively. The adoption did *not* have a material impact on our consolidated financial statements.

In *November 2015*, the FASB issued ASU 2015-17, *Balance Sheet Classification of Deferred Taxes*, which requires the Company to present all deferred tax assets and liabilities as noncurrent. We adopted this ASU on *July 1, 2017* on a prospective basis. At *June 30, 2017* we had net current deferred tax assets of \$3.9 million which would have been classified as noncurrent under the new standard.

In *March 2016*, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*, which amends ASC Topic 718, Stock Compensation. The objective of this amendment is part of the FASB’s Simplification Initiative as it applies to several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. We adopted effective *July 1, 2017*. For the fiscal year ended *June 30, 2018*, the Company recorded a net tax expense of \$0.6 million due to adoption of this ASU. For the fiscal year ended *June 30, 2017*, the Company recorded a credit to additional paid in capital of \$0.1 million, that under the new standard would have been recognized in income.

### **(2) Business Acquisitions**

From time to time the Company acquires design centers from its independent retailers in arms length transactions. There were *no* material acquisitions completed during the *three* fiscal years ended *June 30, 2018, 2017* and *2016*, respectively.

### **(3) Inventories**

Inventories at *June 30* are summarized as follows (in thousands):

|                     | 2018      | 2017      |
|---------------------|-----------|-----------|
| Finished goods      | \$124,640 | \$117,388 |
| Work in process     | 12,057    | 10,638    |
| Raw materials       | 27,947    | 26,269    |
| Valuation allowance | (1,632 )  | (4,812 )  |
| Inventories         | \$163,012 | \$149,483 |

#### (4) Property, Plant and Equipment

Property, plant and equipment at *June 30* are summarized as follows (in thousands):

|                                                 | 2018      | 2017      |
|-------------------------------------------------|-----------|-----------|
| Land and improvements                           | \$82,899  | \$79,200  |
| Building and improvements                       | 404,522   | 400,246   |
| Machinery and equipment                         | 123,606   | 125,773   |
| Property, plant and equipment, gross            | 611,027   | 605,219   |
| Less: accumulated depreciation and amortization | (343,124) | (335,021) |
| Property, plant and equipment, net              | \$267,903 | \$270,198 |

#### (5) Goodwill and Other Intangible Assets

At both *June 30, 2018* and *2017*, we had \$25.4 million of goodwill, and \$19.7 million of other indefinite-lived intangible assets consisting of Ethan Allen trade names, all of which is in our wholesale segment.

In the *fourth* quarter of fiscal years *2018, 2017*, and *2016*, the Company performed qualitative assessments of the fair value of the wholesale reporting unit and concluded it is more likely than *not* that the fair value of its goodwill exceeded its carrying value. The fair value of the trade name exceeded its carrying value by a substantial margin in fiscal years *2018, 2017* and *2016*. To calculate fair value of these assets, management relies on estimates and assumptions which by their nature have varying degrees of uncertainty. Management therefore looks for *third* party transactions to provide the best possible support for the assumptions incorporated. Management considers several factors to be significant when estimating fair value including expected financial outlook of the business, changes in the Company's stock price, the impact of changing market conditions on financial performance and expected future cash flows, and other factors. Deterioration in any of these factors *may* result in a lower fair value assessment, which could lead to impairment of the long-lived assets and goodwill of the Company.





**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES****(6) Debt**

Total debt obligations at *June 30* consist of the following (in thousands):

|                                 | 2018    | 2017     |
|---------------------------------|---------|----------|
| Term Loan due 10/21/2019        | \$-     | \$13,833 |
| Capital leases                  | 1,680   | 1,085    |
| Total debt obligations          | 1,680   | 14,918   |
| Unamortized debt issuance costs | -       | (579 )   |
| Total debt                      | 1,680   | 14,339   |
| Less current maturities         | 584     | 2,731    |
| Total long-term                 | \$1,096 | \$11,608 |

The Company entered into a *five* year, \$150 million senior secured revolving credit and term loan facility on *October 21, 2014*, as amended (the “Facility”). The Company intends to use the Facility for working capital and general corporate purposes, including dividend payments and share repurchases. The Facility, which expires on *October 21, 2019*, provided a term loan of up to \$35 million and a revolving credit line of up to \$115 million, subject to borrowing base availability. We incurred financing costs of \$1.5 million under the Facility, which are being amortized by the interest method, over the remaining life of the Facility.

At the Company’s option, revolving loans under the Facility bear interest, based on the average availability, at an annual rate of either (a) the London Interbank Offered rate (“LIBOR”) plus 1.5% to 1.75%, or (b) the higher of (i) the prime rate, (ii) the federal funds effective rate plus 0.50%, or (iii) LIBOR plus 1.0% plus in each case 0.5% to 0.75%.

The Company pays a commitment fee of 0.15% to 0.25% per annum on the unused portion of the Facility, and fees on issued letters of credit at an annual rate of 1.5% to 1.75% based on the average availability. Certain payments are restricted if the availability under the revolving credit line falls below 20% of the total revolving credit line, and the Company is subject to pro forma compliance with the fixed charge coverage ratio if applicable.

In fiscal 2018 the Company repaid the remaining balance of \$13.8 million on the term loan with excess operating cash. In fiscal 2017 we repaid \$25.0 million of the revolving credit facility with excess operating cash.

The Facility is secured by all property owned, leased or operated by the Company in the United States and includes certain real property owned by the Company and contains customary covenants which *may* limit the Company's ability to incur debt; engage in mergers and consolidations; make restricted payments (including dividends and share repurchases); sell certain assets; and make investments.

The Facility includes a covenant that requires the Company to maintain a minimum fixed charge coverage ratio of *1.1* to *1.0* at all times unless the outstanding term loans are less than \$17.5 million and the fixed charge coverage ratio equals or exceeds *1.25* to *1.0*, in which case the fixed charge coverage ratio ceases to apply and thereafter is only triggered if average monthly availability is less than *15%* of the amount of the revolving credit line. The Company has met the exemption conditions and is currently exempt from the fixed charge coverage ratio covenant.

At *June 30, 2018* and *June 30, 2017*, there was \$6.2 million and \$0.1 million respectively, of standby letters of credit outstanding under the Facility. In fiscal 2018 we issued a \$5.9 million letter of credit for our workmen's compensation obligation in lieu of restricted cash, resulting in reclassification of this restricted cash to cash and cash equivalents. Total availability under the Facility was \$108.8 million at *June 30, 2018* and \$114.9 million at *June 30, 2017*.

At both *June 30, 2018* and *June 30, 2017*, we were in compliance with all covenants under the Facility.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

The weighted-average interest rate applicable under our outstanding debt obligations for each of the last *three* fiscal years were as follows:

|                                | Fiscal Year Ended<br>June 30, |       |       |
|--------------------------------|-------------------------------|-------|-------|
|                                | 2018                          | 2017  | 2016  |
| Weighted-average interest rate | 3.3 %                         | 2.4 % | 2.0 % |

Aggregate scheduled maturities of our debt obligations for each of the *five* fiscal years subsequent to *June 30, 2018*, and thereafter are as follows (in thousands):

| <u>Fiscal Year Ended June 30</u> |         |
|----------------------------------|---------|
| 2019                             | 584     |
| 2020                             | 557     |
| 2021                             | 444     |
| 2022                             | 67      |
| 2023                             | 28      |
| Subsequent to 2023               | -       |
| Total scheduled debt payments    | \$1,680 |

**(7) Leases**

We lease real property and equipment under various operating lease agreements expiring at various times through 2039. Leases covering retail design center locations and equipment *may* require, in addition to stated minimums, contingent rentals based on retail sales or equipment usage. Generally, the leases provide for renewal for various periods at stipulated rates. Future minimum lease payments under non-cancelable operating leases for each of the *five* fiscal years subsequent to *June 30, 2018*, and thereafter are shown in the table below. Also shown are minimum future rentals from subleases, which will partially offset lease payments in the aggregate (in thousands):

| <u>Fiscal Year Ended June 30,</u> | Future<br>Minimum<br>Lease<br>Payments | Future<br>Minimum<br>Sublease<br>Rentals |
|-----------------------------------|----------------------------------------|------------------------------------------|
| 2019                              | \$ 34,391                              | \$ 2,313                                 |

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|                    |            |          |
|--------------------|------------|----------|
| 2020               | 29,231     | \$ 1,800 |
| 2021               | 26,120     | 1,611    |
| 2022               | 22,332     | 1,505    |
| 2023               | 16,866     | 1,077    |
| Subsequent to 2023 | 47,046     | 1,124    |
| Total              | \$ 175,986 | \$ 9,430 |

Total rent expense for each of the past *three* fiscal years ended *June 30* was as follows (in thousands):

|                                           | 2018     | 2017     | 2016     |
|-------------------------------------------|----------|----------|----------|
| Basic rentals under operating leases      | \$33,734 | \$33,033 | \$31,692 |
| Contingent rentals under operating leases | 133      | 142      | 180      |
| Basic and contingent rentals              | 33,867   | 33,175   | 31,872   |
| Less: sublease rent                       | (1,853 ) | (1,824 ) | (1,964 ) |
| Total rent expense                        | \$32,014 | \$31,351 | \$29,908 |

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

Deferred rent credits and deferred lease incentives are reflected in the Consolidated Balance Sheets under the caption other long-term liabilities, and are amortized over the respective underlying lease terms on a straight-line basis as a reduction of rent expense. Amounts recorded are as follows:

|                           | June 30, |          |
|---------------------------|----------|----------|
|                           | 2018     | 2017     |
| Deferred rent credits     | \$13,157 | \$13,876 |
| Deferred lease incentives | \$4,532  | \$5,238  |

### (8) Shareholders' Equity

Our authorized capital stock consists of 150,000,000 shares of Common Stock, par value \$.01 per share, and 1,055,000 shares of Preferred Stock, par value \$.01 per share. The Board of Directors *may* provide for the issuance of all or any shares of Preferred Stock in *one* or more classes or series, and to fix for each such class or series such voting powers, full or limited, or *no* voting powers, and such distinctive designations, preferences and relative, participating, optional or other special rights and such qualifications, limitations or restrictions thereof, as shall be stated and expressed in the resolution or resolutions adopted by the Board of Directors providing for the issuance of such class or series and as *may* be permitted by the General Corporation Law of the State of Delaware. As of *June 30, 2018* and *2017*, there were *no* shares of Preferred Stock issued or outstanding.

#### Share Repurchase Program

On *November 21, 2002*, our Board of Directors approved a share repurchase program authorizing us to repurchase up to 2.0 million shares of our common stock, from time to time, either directly or through agents, in the open market at prices and on terms satisfactory to us. After that date, the Board of Directors increased the aggregate authorization under the repurchase program on several separate occasions, the last of which was on *April 24, 2018* when the Board of Directors increased the aggregate authorization to approximately 3.0 million shares. There is *no* expiration date on the repurchase authorization and the amount and timing of future share repurchases, if any, will be determined as market and business conditions warrant. As of *June 30, 2018* we had a remaining Board authorization to repurchase 2.5 million shares.

During the past *three* fiscal years, we repurchased the following shares of our common stock (trade date basis):

|                                  | 2018         | 2017         | 2016         |
|----------------------------------|--------------|--------------|--------------|
| Common shares repurchased        | 950,484      | 357,363      | 697,799      |
| Cost to repurchase common shares | \$22,019,381 | \$10,246,302 | \$19,346,104 |
| Average price per share          | \$23.17      | \$28.67      | \$27.72      |

For the fiscal years presented above, we funded our purchases of treasury stock with existing cash on hand, cash generated through current period operations, and our credit facility. All our common stock repurchases are recorded as treasury stock and result in a reduction of shareholders' equity.

### (9) Earnings per Share (in thousands)

The following table sets forth the calculation of weighted average shares for the fiscal years ended *June 30*:

|                                                                                       | 2018   | 2017   | 2016   |
|---------------------------------------------------------------------------------------|--------|--------|--------|
| Weighted average shares of common stock outstanding for basic calculation             | 27,321 | 27,679 | 28,072 |
| Effect of dilutive stock options and other share-based awards                         | 304    | 279    | 252    |
| Weighted average shares of common stock outstanding adjusted for dilution calculation | 27,625 | 27,958 | 28,324 |

In 2018, 2017 and 2016, stock options and share based awards of 195, 379 and 460 respectively, were excluded from earnings per share calculation because their impact is anti-dilutive.

### (10) Share-Based Compensation

For the *twelve* months ended *June 30*, 2018, 2017, and 2016, share-based compensation expense totaled \$1.0 million, \$1.3 million, and \$2.4 million respectively. These amounts have been included in the Consolidated Statements of Comprehensive Income within selling, general and administrative expenses. During the *twelve* months ended *June 30*, 2018, 2017, and 2016, we recognized related tax benefits associated with our share-based compensation arrangements totaling \$0.5 million, \$0.5 million and \$0.8 million, respectively (before valuation allowances). Such amounts have been included in the Consolidated Statements of Comprehensive Income within income tax expense.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

At *June 30, 2018*, we had *1,447,639* shares of common stock available for future issuance pursuant to the *1992* Stock Option Plan (the “Plan”). The maximum number of shares of common stock reserved for issuance under the Plan is *6,487,867* shares. The Plan provides for the grant of non-compensatory stock options to eligible employees and non-employee directors. Stock options under the Plan are non-qualified under section *422* of the Internal Revenue Code and allow for the purchase of shares of our common stock. The Plan also provides for the issuance of stock appreciation rights (“SARs”) on issued options, however *no* SARs have been issued to date. The awarding of such options is determined by the Compensation Committee of the Board of Directors after consideration of recommendations proposed by the Chief Executive Officer. Options are generally granted with an exercise price equal to the market price of our common stock at the date of grant, vest ratably over a specified service period, and have a contractual term of *10* years. Equity awards can also include performance vesting conditions. Company policy further requires an additional *one* year holding period beyond the service vest date for certain executives. Beginning *January 31, 2014*, grants to employees include both company performance and service vesting conditions (as further described below). Grants to independent directors have a *3*-year service vesting condition. Following is a description of grants made under the Plan.

Stock Option Awards

We estimate, as of the date of grant, the fair value of stock options awarded using the Black-Scholes option pricing model. Use of a valuation model requires management to make certain assumptions with respect to selected model inputs, including anticipated changes in the underlying stock price (i.e. expected volatility) and option exercise activity (i.e. expected life). Expected volatility is based on the historical volatility of our stock. The risk-free rate of return is based on the U.S. Treasury bill rate extrapolated to the term matching the expected life of the grant. The dividend yield is based on the annualized dividend rate at the grant date relative to the grant date stock price. The expected life of options granted, which represents the period of time that the options are expected to be outstanding, is based, primarily, on historical data. The weighted average assumptions used for fiscal years ended *June 30* are noted in the following table:

|                               | 2018  | 2017  | 2016  |
|-------------------------------|-------|-------|-------|
| Volatility                    | 31.5% | 36.8% | 48.1% |
| Risk-free rate of return      | 1.76% | 1.03% | 1.93% |
| Dividend yield                | 2.47% | 1.96% | 1.95% |
| Expected average life (years) | 4.6   | 5.0   | 6.3   |

Options granted to employees beginning *January 1, 2014* vest provided certain performance and service conditions are met (“Performance Options”). The performance conditions allow the potential vesting in *three* equal tranches, provided attainment of a minimum annual *5%* growth in operating income (as defined in the agreement) for each of the ensuing *three* fiscal years. If the minimum annual growth is *not* achieved in any fiscal year, that tranche is

forfeited, except that if a cumulative compound growth rate of 5% is achieved at the end of the *three* fiscal years, performance conditions for all *three* tranches will have been met. Service conditions require an additional period after performance conditions are met. Consequently, assuming both performance and service conditions are met, shares become exercisable between 3 and 5 years from grant date. At *June 30, 2017*, 196,000 Performance Options achieved the performance conditions, and consequently will vest ratably in *three* equal tranches on the grant date anniversary in years three, *four* and *five* provided service conditions are also met. The remaining 130,000 Performance Options did *not* achieve the respective performance conditions so the amortization to date was reversed at *June 30, 2017*, and the options were cancelled during fiscal 2018. The Performance Options are reflected in the options tables presented below. All options were issued at the closing stock price on each grant date, and have a contractual term of 10 years. A summary of stock option activity occurring during the fiscal year ended *June 30, 2018* is presented below.

| <u>Options</u>               | Shares    | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term (yrs) | Aggregate<br>Intrinsic<br>Value |
|------------------------------|-----------|------------------------------------------|---------------------------------------------------------------|---------------------------------|
| Outstanding - June 30, 2017  | 836,020   | \$ 24.41                                 |                                                               |                                 |
| Granted                      | 19,482    | 30.80                                    |                                                               |                                 |
| Exercised                    | (9,066 )  | 21.37                                    |                                                               |                                 |
| Canceled (forfeited/expired) | (284,841) | 30.28                                    |                                                               |                                 |
| Outstanding - June 30, 2018  | 561,595   | 21.70                                    | 3.7                                                           | \$2,205,554                     |
| Exercisable - June 30, 2018  | 453,423   | \$ 20.25                                 | 2.9                                                           | \$2,205,554                     |



**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

The weighted average grant-date fair value of options granted during fiscal 2018, 2017 and 2016 was \$6.93, \$8.30 and \$11.53 respectively. The total intrinsic value of options exercised during fiscal 2018, 2017 and 2016 was \$0.1 million, \$0.8 million, and \$0.3 million, respectively. As of *June 30, 2018*, there was \$0.3 million of total unrecognized compensation cost related to nonvested options granted under the Plan. That cost is expected to be recognized over a weighted average period of 1.4 years. A summary of the nonvested shares as of *June 30, 2018* and changes during the year then ended is presented below.

| <u>Options</u>               | Shares    | Weighted<br>Average<br>Grant<br>Date Fair<br>Value |
|------------------------------|-----------|----------------------------------------------------|
| Nonvested June 30, 2017      | 285,284   | \$ 11.18                                           |
| Granted                      | 19,482    | 6.93                                               |
| Vested                       | (69,219 ) | 10.99                                              |
| Canceled (forfeited/expired) | (127,375) | 11.40                                              |
| Nonvested at June 30, 2018   | 108,172   | \$ 10.27                                           |

Stock Unit Awards

We account for stock unit awards as equity-based awards because upon vesting, they will be settled in common shares. These awards, which contain time and other vesting conditions, *may* also contain performance conditions providing recipients a contingent right to receive shares of the Company's common stock ("Performance Units"), conditioned upon the Company's achievement of certain performance targets and goals, and subject to the terms of the agreements. For Performance Units, we expense as compensation cost the fair value of the shares as of the grant date, and amortize expense ratably over the total performance and time vest period, taking into account the probability that we will satisfy the performance goals. We estimate, as of the date of grant, the fair value of Performance Units with a discounted cash flow model, using as model inputs the risk-free rate of return as the discount rate, dividend yield for dividends *not* paid during the restriction period, and a discount for lack of marketability for a *one*-year post-vest holding period. The lack of marketability discount used is the present value of a future put option using Monte-Carlo and Black-Scholes pricing models. The weighted average assumptions used for the fiscal years ended *June 30* are noted in the table following. *No* Performance based restricted stock unit awards were granted under the Plan prior to *December 1, 2015*.

|                          | 2018  | 2017  |
|--------------------------|-------|-------|
| Volatility               | 32.9% | 30.8% |
| Risk-free rate of return | 1.41% | 0.92% |

|                               |       |       |
|-------------------------------|-------|-------|
| Dividend yield                | 2.47% | 1.97% |
| Expected average life (years) | 1.91  | 2.04  |

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

For each grant of Performance Units, the amount of the grant that will be earned and paid will be determined by reference to the achievement of certain performance goals applicable to such grant. Equity-based compensation expenses related to performance-based shares recognized in our consolidated statements of comprehensive income are presented in the following table for the fiscal years ended *June 30* (in thousands).

|                                                            |       |       |
|------------------------------------------------------------|-------|-------|
| Granted<br>within<br>fiscal<br>years<br>ending<br>June 30, | 2018  | 2017  |
| 2016                                                       | \$92  | \$794 |
| 2017                                                       | (12)  | 12    |
| 2018                                                       | 457   | -     |
| Total<br>expense                                           | \$537 | \$806 |

A summary of stock unit activity occurring during the fiscal year ended *June 30, 2018* is presented below.

|                              | Units    | Weighted<br>Average<br>Grant<br>Date<br>Fair<br>Value |
|------------------------------|----------|-------------------------------------------------------|
| Nonvested June 30, 2017      | 308,330  | \$ 25.92                                              |
| Granted                      | 162,500  | 25.18                                                 |
| Vested                       | (59,211) | 23.96                                                 |
| Canceled (forfeited/expired) | (81,250) | 24.94                                                 |
| Nonvested at June 30, 2018   | 330,369  | \$ 26.15                                              |

As of *June 30, 2018*, there was \$0.6 million of total unrecognized compensation cost related to nonvested units granted under the Plan based on our probability estimates. That cost is expected to be recognized over a weighted average period of 1 year.

Restricted Stock Awards

A summary of stock unit activity occurring during the fiscal year ended *June 30, 2018* is presented below.

|                              | Units    | Weighted<br>Average<br>Grant<br>Date<br>Fair<br>Value |
|------------------------------|----------|-------------------------------------------------------|
| Nonvested June 30, 2017      | -        | \$ -                                                  |
| Granted                      | 16,234   | 25.62                                                 |
| Vested                       | -        | -                                                     |
| Canceled (forfeited/expired) | (16,234) | (25.62 )                                              |
| Nonvested at June 30, 2018   | -        | \$ -                                                  |

During fiscal 2018 16,234 restricted stock awards were granted and then subsequently voided. There was *no* unrecognized compensation cost related to restricted shares granted under the Plan for fiscal 2018.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES****(11) Income Taxes**

Income tax expense attributable to income from operations consists of the following for the fiscal years ended *June 30* (in thousands):

|                              | 2018     | 2017     | 2016     |
|------------------------------|----------|----------|----------|
| Current:                     |          |          |          |
| Federal                      | \$10,289 | \$15,265 | \$27,660 |
| State                        | 1,689    | 1,585    | 2,898    |
| Foreign                      | 824      | 445      | 88       |
| Total current                | 12,802   | 17,295   | 30,646   |
| Deferred:                    |          |          |          |
| Federal                      | 174      | 3,413    | (237 )   |
| State                        | (124 )   | 85       | 207      |
| Foreign                      | (156 )   | 8        | 703      |
| Total deferred               | (106 )   | 3,506    | 673      |
| Income Tax Expense (Benefit) | \$12,696 | \$20,801 | \$31,319 |

The following is a reconciliation of expected income tax expense (benefit) (computed by applying the federal statutory income tax rate to income before taxes) to actual income tax expense (benefit) (in thousands):

|                                                       | 2018     |        | 2017     |        | 2016     |        |
|-------------------------------------------------------|----------|--------|----------|--------|----------|--------|
| Expected Income Tax Expense                           | \$13,739 | 28.0%  | \$19,947 | 35.0%  | \$30,785 | 35.0%  |
| State income taxes, net of federal income tax         | 1,263    | 2.6 %  | 1,403    | 2.5 %  | 2,514    | 2.9 %  |
| Valuation allowance                                   | 42       | 0.1 %  | 329      | 0.6 %  | 339      | 0.4 %  |
| Re-measurement of deferred taxes                      | (2,651 ) | -5.4 % | -        | -      | -        | -      |
| Section 199 Qualified Production Activities deduction | (678 )   | -1.4 % | (999 )   | -1.8 % | (1,513 ) | -1.7 % |
| Unrecognized tax expense (benefit)                    | 55       | 0.1 %  | (48 )    | -0.1 % | (479 )   | -0.5 % |
| Stock compensation - Cancellations & exercises        | 570      | 1.2 %  | -        | -      | -        | -      |
| Other, net                                            | 356      | 0.7 %  | 169      | 0.3 %  | (327 )   | -0.4 % |
| Actual income tax expense (benefit)                   | \$12,696 | 25.9%  | \$20,801 | 36.5%  | \$31,319 | 35.6%  |

The deferred income tax asset and liability balances at *June 30* (in thousands) include:

|                                  | 2018     | 2017     |
|----------------------------------|----------|----------|
| Deferred tax assets:             |          |          |
| Employee compensation accruals   | 2,729    | 4,395    |
| Stock based compensation         | 933      | 2,878    |
| Deferred rent credits            | 4,407    | 7,290    |
| Net operating loss carryforwards | 3,959    | 3,687    |
| Inventories                      | 62       | 1,254    |
| Goodwill                         | 328      | 953      |
| Other, net                       | 1,645    | 2,396    |
| Total deferred tax assets        | 14,063   | 22,853   |
| Less: Valuation allowance        | (2,527 ) | (2,485 ) |
| Net deferred tax assets          | \$11,536 | \$20,368 |

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

|                                          | 2018       | 2017       |
|------------------------------------------|------------|------------|
| Deferred tax liabilities:                |            |            |
| Property, plant and equipment            | 2,827      | 5,360      |
| Intangible assets other than goodwill    | 8,951      | 14,166     |
| Commissions                              | 2,230      | 3,420      |
| Total deferred tax liability             | 14,008     | 22,946     |
| Total net deferred tax asset (liability) | \$(2,472 ) | \$(2,578 ) |

The deferred tax balances are classified in the Consolidated Balance Sheets as follows at *June 30* (in thousands):

|                                          | 2018       | 2017       |
|------------------------------------------|------------|------------|
| Current assets                           | -          | \$3,916    |
| Non-current assets                       | 1,688      | 1,167      |
| Current liabilities                      | -          | -          |
| Non-current liabilities                  | 4,160      | 7,661      |
| Total net deferred tax asset (liability) | \$(2,472 ) | \$(2,578 ) |

Commencing with fiscal *2018* the Company is prospectively reporting its deferred tax assets and liabilities as non-current in conformance with ASU *2015-17* “Balance Sheet Classification of Deferred Tax Assets. For fiscal *2017*, current deferred tax assets and liabilities and non-current deferred tax assets and liabilities have been presented net in the Consolidated Balance Sheets.

We evaluate our deferred taxes to determine if the “more likely than *not*” standard of evidence has *not* been met thereby supporting the need for a valuation allowance. A valuation allowance must be established for deferred tax assets when it is less than *50%* likely that assets will be realized. At *June 30* of *2018* and *2017*, such an allowance was in place against the Belgian foreign tax assets, and at *June 30, 2018* this valuation allowance was approximately \$2.6 million.

The Company’s deferred income tax assets at *June 30, 2018* with respect to the net operating losses expire as follows (in thousands):

|          |               |
|----------|---------------|
| Deferred | Net Operating |
| Income   | Loss          |
|          | Carryforwards |

|                                                       | Tax      |           |
|-------------------------------------------------------|----------|-----------|
|                                                       | Assets   |           |
| United States (State), expiring between 2025 and 2032 | \$ 1,340 | \$ 23,831 |
| Foreign, expiring between 2034 and 2038               | 2,619    | 7,745     |

Deferred U.S. federal income taxes were previously *not* provided for unremitted foreign earnings of our foreign subsidiaries because we expected those earnings to be permanently reinvested. As part of the Tax Act the Company must report The Deemed Repatriation Transition Tax (the “Transition Tax”) on previously untaxed accumulated earnings and profits (“E&P”) of certain of our foreign subsidiaries. To determine the amount of the Transition Tax, we must determine, in addition to other factors, the amount of post-1986 E&P of the relevant subsidiaries, as well as the amount of non-U.S. income taxes paid on such earnings. We are able to make a reasonable estimate and recorded a provisional Transition Tax obligation of \$125K.

On *December 22, 2017* H.R. 1, originally known as the Tax Cuts and Jobs Act, (the “Tax Act”) was enacted. Among the significant changes to the U.S. Internal Revenue Code, the Tax Act lowers the U.S. federal corporate income tax rate (“Federal Tax Rate”) from 35% to 21% effective *January 1, 2018*, introduces a limitation on the deduction of certain interest expenses, introduces a deduction for certain business capital expenditures and introduces a system of taxing foreign-sourced income from multinational corporations. The Company will compute its income tax expense for the *June 30, 2018* fiscal year using a blended Federal Tax Rate of 28%. The 21% Federal Tax Rate will apply to fiscal years ending *June 30, 2019* and each year thereafter.



**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

The Company must re-measure its net deferred tax assets and liabilities using the Federal Tax Rate that will apply when these amounts are expected to reverse. As of *June 30, 2018*, the Company can determine a reasonable estimate for the effects of tax reform. The re-measurement of the deferred tax assets and liabilities resulted in a discrete tax benefit \$2.7 million at *June 30, 2017* which lowered the effective tax rate by 5.4% for the fiscal year.

Uncertain Tax Positions

We recognize interest and penalties related to income tax matters as a component of income tax expense. If the \$2.2 million of unrecognized tax benefits and related interest and penalties as of *June 30, 2018* were recognized, approximately \$1.7 million would be recorded as a benefit to income tax expense. A reconciliation of the beginning and ending amount of unrecognized tax benefits including related interest and penalties as of *June 30, 2018* and *2017* is as follows (in thousands):

|                                                   | 2018    | 2017    |
|---------------------------------------------------|---------|---------|
| Beginning balance                                 | \$2,106 | \$2,170 |
| Additions for tax positions taken                 | 467     | 646     |
| Reductions for tax positions taken in prior years | (386 )  | (694 )  |
| Settlements                                       | -       | (16 )   |
| Ending balance                                    | \$2,187 | \$2,106 |

It is reasonably possible that various issues relating to approximately \$0.3 million of the total gross unrecognized tax benefits as of *June 30, 2018* will be resolved within the next *twelve* months as exams are completed or statutes expire. If recognized, approximately \$0.1 million of unrecognized tax benefits would reduce our tax expense in the period realized. However, actual results could differ from those currently anticipated.

The Company conducts business globally and, as a result, the Company or *one* or more of its subsidiaries files income tax returns in the U.S., various state, and foreign jurisdictions. In the normal course of business, the Company is subject to examination by the taxing authorities in such major jurisdictions as the U.S. Canada, Mexico, Belgium and Honduras. As of *June 30, 2018*, the Company and certain subsidiaries are currently under audit from *2015* through *2016* in the U.S. While the amount of uncertain tax benefits with respect to the entities and years under audit *may* change within the next *twelve* months, it is *not* anticipated that any of the changes will be significant.

## **(12) Employee Retirement Programs**

### The Ethan Allen Retirement Savings Plan

The Ethan Allen Retirement Savings Plan (the "Savings Plan") is a defined contribution plan, which is offered to substantially all our employees who have completed *three* consecutive months of service regardless of hours worked. We *may*, at our discretion, make a matching contribution to the 401(k) portion of the Savings Plan on behalf of each participant. Total 401(k) Company match expense amounted to \$3.4 million in 2018, \$3.5 million in 2017, and \$3.4 million in 2016.

### Other Retirement Plans and Benefits

Ethan Allen provides additional benefits to selected members of senior and middle management in the form of previously entered deferred compensation arrangements and a management cash bonus and other incentive programs. The total cost of these benefits was \$0.1 million, \$1.0 million, and \$3.6 million in 2018, 2017 and 2016, respectively.

## **(13) Litigation**

We are routinely party to various legal proceedings, including investigations or as a defendant in litigation, in the ordinary course of business. We are also subject to various federal, state and local environmental protection laws and regulations and are involved, from time to time, in investigations and proceedings regarding environmental matters. Such investigations and proceedings typically concern air emissions, water discharges, and/or management of solid and hazardous wastes. Under these laws, we and/or our subsidiaries are, or *may* be, required to remove or mitigate the effects on the environment of the disposal or release of certain hazardous materials.

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

Regulations issued under the Clean Air Act Amendments of 1990 required the industry to reformulate certain furniture finishes or institute process changes to reduce emissions of volatile organic compounds. Compliance with many of these requirements has been facilitated through the introduction of high solids coating technology and alternative formulations. In addition, we have instituted a variety of technical and procedural controls, including reformulation of finishing materials to reduce toxicity, implementation of high velocity low pressure spray systems, development of storm water protection plans and controls, and further development of related inspection/audit teams, all of which have served to reduce emissions per unit of production. We remain committed to implementing new waste minimization programs and/or enhancing existing programs with the objective of (i) reducing the total volume of waste, (ii) limiting the liability associated with waste disposal, and (iii) continuously improving environmental and job safety programs on the factory floor which serve to minimize emissions and safety risks for employees. To reduce the use of hazardous materials in the manufacturing process, we will continue to evaluate the most appropriate, cost-effective control technologies for finishing operations and production methods. We believe that our facilities are in material compliance with all such applicable laws and regulations. Our currently anticipated capital expenditures for environmental control facility matters are *not* material.

On a quarterly basis, we review our litigation activities and determine if an unfavorable outcome to us is considered “remote”, “reasonably possible” or “probable” as defined by ASC 450 – *Contingencies*. Where we determine an unfavorable outcome is probable and is reasonably estimable, we accrue for potential litigation losses. The liability we *may* ultimately incur with respect to such litigation matters, in the event of a negative outcome, *may* be in excess of amounts currently accrued, if any; however, we do *not* expect that the reasonably possible outcome of these litigation matters would, individually or in the aggregate, have a material adverse effect on our financial condition, results of operations or cash flows. Where we determine an unfavorable outcome is *not* probable or reasonably estimable, we do *not* accrue for any potential litigation loss.

Although the outcome of the various claims and proceedings against us cannot be predicted with certainty, management believes that the likelihood is remote that any existing claims or proceedings, individually or in the aggregate, will have a material adverse effect on our financial position, results of operations or cash flows.

### **(14) Accumulated Other Comprehensive Income (Loss)**

The following table sets forth the activity in accumulated other comprehensive income (loss) for the fiscal years ended *June 30* (in thousands):

|                                                                  | Years ended June<br>30, |           |
|------------------------------------------------------------------|-------------------------|-----------|
|                                                                  | 2018                    | 2017      |
| Beginning balance                                                | \$(4,131)               | \$(4,846) |
| Changes before reclassifications                                 | (2,040)                 | 715       |
| Amounts reclassified from accumulated other comprehensive income | -                       | -         |
| Current period other comprehensive income (loss)                 | (2,040)                 | 715       |
| Ending balance                                                   | \$(6,171)               | \$(4,131) |

Foreign currency translation adjustments are the result of changes in foreign currency exchange rates related to our operations in Canada, Belgium, Honduras and Mexico, and exclude income taxes given that the earnings of non-U.S. subsidiaries are deemed to be reinvested for an indefinite period.

### **(15) Segment Information**

Our wholesale and retail operating segments represent strategic business areas of our vertically integrated enterprise that operate separately and provide their own distinctive services. This vertical structure enables us to offer our complete line of home furnishings and accents more effectively while controlling quality and cost. We evaluate performance of the respective segments based upon revenues and operating income. Inter-segment transactions result, primarily, from the wholesale sale of inventory to the retail segment, including the related profit margin.

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

As of *June 30, 2018*, the Company operated *148* design centers (our retail segment) and our independent retailers operated *148* design centers. Our wholesale segment net sales include sales to our retail segment, which are eliminated in consolidation, and sales to our independent retailers. Our retail segment net sales accounted for 77% of our consolidated net sales in fiscal 2018. Our wholesale segment net sales to independent retailers and other *third* parties accounted for 23%, including approximately 15.5% of our consolidated net sales in fiscal 2018 to our *ten* largest customers, including the GSA and *nine* independent retailers who operate *105* design centers. Information for each of the last *three* fiscal years ended *June 30* is provided below (in thousands):

|                                    | 2018      | 2017      | 2016      |
|------------------------------------|-----------|-----------|-----------|
| <u>Net sales:</u>                  |           |           |           |
| Wholesale segment                  | \$475,731 | \$453,326 | \$491,467 |
| Retail segment                     | 587,502   | 603,677   | 626,511   |
| Elimination of inter-company sales | (296,449) | (293,618) | (323,776) |
| Consolidated Total                 | \$766,784 | \$763,385 | \$794,202 |

|                                        |          |          |          |
|----------------------------------------|----------|----------|----------|
| <u>Operating income (loss):</u>        |          |          |          |
| Wholesale segment                      | \$48,499 | \$53,505 | \$74,412 |
| Retail segment                         | (1,738 ) | 1,198    | 16,450   |
| Adjustment of inter-company profit (1) | 2,106    | 3,247    | (1,683 ) |
| Consolidated Total                     | \$48,867 | \$57,950 | \$89,179 |

|                                         |          |          |          |
|-----------------------------------------|----------|----------|----------|
| <u>Depreciation &amp; Amortization:</u> |          |          |          |
| Wholesale segment                       | \$7,752  | \$7,550  | \$7,587  |
| Retail segment                          | 12,079   | 12,565   | 11,766   |
| Consolidated Total                      | \$19,831 | \$20,115 | \$19,353 |

|                              |          |          |          |
|------------------------------|----------|----------|----------|
| <u>Capital expenditures:</u> |          |          |          |
| Wholesale segment            | \$4,286  | \$8,589  | \$12,446 |
| Retail segment               | 14,487   | 9,732    | 10,686   |
| Consolidated Total           | \$18,773 | \$18,321 | \$23,132 |

|                                  | June 30,<br>2018 | June 30,<br>2017 | June 30,<br>2016 |
|----------------------------------|------------------|------------------|------------------|
| <u>Total Assets:</u>             |                  |                  |                  |
| Wholesale segment                | \$241,616        | \$279,364        | \$271,116        |
| Retail segment                   | 317,590          | 319,341          | 339,942          |
| Inventory profit elimination (2) | (28,773 )        | (30,483 )        | (33,649 )        |
| Consolidated Total               | \$530,433        | \$568,222        | \$577,409        |

(1)

Represents the change in wholesale profit contained in Ethan Allen design center inventory at the end of the period.

- (2) The wholesale profit contained in the retail segment inventory that has *not* yet been realized. These profits are realized when the related inventory is sold.

Our international net sales are comprised of our wholesale segment sales to independent retailers and our retail segment sales to consumers through the Company operated design centers. The number of international design centers, and the related net sales as a percent of our consolidated net sales is shown in the following table.

|                                      | Fiscal Year Ended<br>June 30, |       |       |
|--------------------------------------|-------------------------------|-------|-------|
|                                      | 2018                          | 2017  | 2016  |
| Independent design centers           | 104                           | 107   | 103   |
| Company operated design centers      | 6                             | 6     | 6     |
| Total international design centers   | 110                           | 113   | 109   |
| Percentage of consolidated net sales | 10.2%                         | 10.0% | 9.2 % |

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES****(16) Selected Quarterly Financial Data (Unaudited)**

Tabulated below is selected financial data for each quarter of the fiscal years ended *June 30, 2018, 2017, and 2016* (in thousands, except per share data):

|                                     | Quarter Ended   |                |           |           |
|-------------------------------------|-----------------|----------------|-----------|-----------|
|                                     | September<br>30 | December<br>31 | March 31  | June 30   |
| <u>Fiscal 2018:</u>                 |                 |                |           |           |
| Net Sales                           | \$181,302       | \$198,481      | \$181,419 | \$205,582 |
| Gross profit                        | 100,323         | 107,791        | 96,708    | 111,142   |
| Net income                          | 7,415           | 14,862         | 2,616     | 11,478    |
| Earnings per basic share            | 0.27            | 0.54           | 0.10      | 0.43      |
| Earnings per diluted share          | 0.27            | 0.54           | 0.09      | 0.42      |
| Dividends declared per common share | 0.19            | 0.50           | 0.19      | 0.19      |
| <u>Fiscal 2017:</u>                 |                 |                |           |           |
| Net Sales                           | \$193,287       | \$194,672      | \$180,501 | \$194,925 |
| Gross profit                        | 108,467         | 108,124        | 94,735    | 108,397   |
| Net income                          | 11,529          | 10,700         | 2,282     | 11,683    |
| Earnings per basic share            | 0.42            | 0.39           | 0.08      | 0.42      |
| Earnings per diluted share          | 0.41            | 0.38           | 0.08      | 0.42      |
| Dividends declared per common share | 0.17            | 0.19           | 0.19      | 0.19      |
| <u>Fiscal 2016:</u>                 |                 |                |           |           |
| Net Sales                           | \$190,391       | \$207,535      | \$190,583 | \$205,693 |
| Gross profit                        | 104,673         | 116,058        | 105,717   | 115,788   |
| Net income                          | 13,147          | 16,534         | 10,178    | 16,778    |
| Earnings per basic share            | 0.46            | 0.58           | 0.37      | 0.60      |
| Earnings per diluted share          | 0.46            | 0.58           | 0.36      | 0.60      |
| Dividends declared per common share | 0.14            | 0.14           | 0.17      | 0.17      |

**(17) Financial Instruments**

At *June 30, 2017*, \$7.3 million of cash equivalents were restricted and classified as a long-term asset. We did *not* hold any restricted cash equivalents at *June 30, 2018*. We did *not* hold any available-for-sale securities at *June 30, 2018* and *June 30, 2017*.

We measure certain assets, including our cost and equity method investments, at fair value on a nonrecurring basis. These assets are recognized at fair value when they are deemed to be other-than-temporarily impaired. During the year ended *June 30, 2018* we did *not* record any other-than-temporary impairments on those assets required to be measured at fair value on a non-recurring basis.

**(18) Restricted Cash and Investments**

At *June 30, 2017* we held \$7.3 million of cash and investments in lieu of providing letters of credit for the benefit of the provider of our workmen's compensation and other insurance liabilities. By *June 30, 2018*, this obligation had been reduced to \$5.9 million, which was then exchanged for a letter of credit for the benefit of this provider, and the restrictions were removed. See also Note 17, "Financial Instruments".

**(19) Subsequent Events**

*None.*

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

*None.*



## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **Item 9A. Controls and Procedures**

#### **Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chairman of the Board and Chief Executive Officer ("CEO") and Executive Vice President Administration and Chief Financial Officer("CFO"), as appropriate, to allow timely decisions regarding required financial disclosure.

We carried out an evaluation, under the supervision and with the participation of our management, including the CEO and the CFO, of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on such evaluation, the CEO and CFO have concluded that, as of June 30, 2018, our disclosure controls and procedures were effective in ensuring that material information relating to us (including our consolidated subsidiaries), which is required to be disclosed by us in our periodic reports filed or submitted to the SEC is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (ii) accumulated and communicated to management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

#### **Management's Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as such term is defined in Exchange Act Rule 13a-15(f) and 15d-15(f)). Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. GAAP.

Our internal control over financial reporting includes those policies and procedures that:

-

pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;

provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. GAAP, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on our financial statements.

Management has assessed the effectiveness of our internal control over financial reporting based on the framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework). Based on that evaluation, management concluded that our internal control over financial reporting was effective as of June 30, 2018 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external reporting purposes in accordance with U.S. GAAP.

KPMG LLP, the independent registered public accounting firm that audited the consolidated financial statements included in this Annual Report on Form 10-K, has also audited the effectiveness of our internal control over financial reporting as of June 30, 2018, as stated in their report included under Item 8 of this Annual Report.

### **Changes in Internal Control over Financial Reporting**

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

### **Item 9B. Other Information**

None.

## **ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

### **PART III**

Except as set forth below, the information required by Items 10, 11, 12, 13 and 14 is incorporated by reference to Ethan Allen Interiors Inc. proxy statement for the Annual Meeting of Shareholders scheduled to be held on November 14, 2018 (the "Proxy Statement") to be filed with the SEC pursuant to Regulation 14A within 120 days after the end of our 2018 fiscal year.

#### **Item 10. Directors, Executive Officers and Corporate Governance**

##### **Code of Ethics**

We have adopted a code of ethics that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. Our code of ethics can be accessed via our website at [www.ethanallen.com/governance](http://www.ethanallen.com/governance).

We intend to disclose any amendment of our Code of Ethics, or any waiver of any provision thereof, applicable to our principal executive officer and/or principal financial officer, or persons performing similar functions, directors and other executive officers on our website within 4 days of the date of such amendment or waiver. In the case of a waiver, the nature of the waiver, the name of the person to whom the waiver was granted, and the date of the waiver will also be disclosed.

Information contained on, or connected to, our website is not incorporated by reference into this Form 10-K and should not be considered part of this or any other report that we file with, or furnish to, the SEC.

##### **Identification of Executive Officers**

The information set forth under the heading "Executive Officers of the Registrant" in Part I, Item 1 of this form 10-K is also incorporated by reference in this section.

##### **Audit Committee Financial Expert**

Our Board of Directors has determined that we have three "audit committee financial experts", as defined under Item 407(d)(5)(ii) of Regulation S-K of the Securities Exchange Act of 1934, currently serving on our Audit Committee. Those members of our Audit Committee who are deemed to be audit committee financial experts are as follows:

James B. Carlson  
Domenick J. Esposito  
James W. Schmotter

All persons identified as audit committee financial experts are independent from management as defined by the applicable listing standards of the New York Stock Exchange.

The remaining information required by this Item will be included in and is incorporated herein by reference from our 2018 Proxy Statement.

#### **Item 11. Executive Compensation**

The information required by this Item will be included in and is incorporated herein by reference from our 2018 Proxy Statement.

#### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters**

The information required by this Item is incorporated by reference to the sections entitled ["Equity Compensation Plan Information"] and ["Security Ownership of Common Stock of Certain Owners and Management"] in the 2018 Proxy Statement.

#### **Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by this Item is incorporated by reference to the section entitled ["Certain Relationships and Related Party Transactions"] and ["Corporate Governance —Director Independence "] in the 2018 Proxy Statement.

#### **Item 14. Principal Accounting Fees and Services**

The information required by this item is incorporated by reference to the sections entitled ["Audit Fees"] and ["Audit and Non-Audit Engagement Pre-Approval Policy "] in the 2018 Proxy Statement.

## **PART IV**

### **Item 15. Exhibits and Financial Statement Schedules**

(a)(1) *Financial Statements.* Our Consolidated Financial Statements, included under Item 8 hereof, as required at June 30, 2018 and 2017, and for the years ended June 30, 2018, 2017 and 2016 consist of the following:

Consolidated Balance Sheets

Consolidated Statements of Comprehensive Income

Consolidated Statements of Cash Flows

**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

Consolidated Statements of Shareholders' Equity

Notes to the Consolidated Financial Statements

(a)(2) *Financial Statement Schedules*. None.

(b) The following Exhibits are filed as part of this report on Form 10-K:

Exhibit

Exhibit

Number

- |         |                                                                                                                                                                                                                                                                                                                                                                                             |
|---------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3 (a)   | <u>Amended and Restated Certificate of Incorporation of the Company dated as of November 16, 2016 (incorporated by reference to Exhibit 3.(A) to the Current Report on Form 8-K of the Company filed with the SEC on November 18, 2016)</u>                                                                                                                                                 |
| 3 (b)   | <u>Certificate of Designations relating to the New Convertible Preferred Stock dated as of March 23, 1993 (incorporated by reference to Exhibit 3(b) to the Annual Report on Form 10-K of the Company filed with the SEC on August 12, 2015)</u>                                                                                                                                            |
| 3 (c)   | <u>Certificate of Designations of Series C Junior Participating Preferred Stock dated as of July 3, 1996, and Certificate of Amendment of Certificate of Designations of Series C Junior Participating Preferred Stock dated as of December 27, 2004 (incorporated by reference to Exhibit 3(c) to the Annual Report on Form 10-K of the Company filed with the SEC on August 12, 2015)</u> |
| 3 (d)   | <u>Amended and Restated By-laws of the Company (incorporated by reference to Exhibit 3.(D) to the Current Report on Form 8-K of the Company filed with the SEC on November 18, 2016)</u>                                                                                                                                                                                                    |
| 3 (e)   | <u>Certificate of Incorporation of Ethan Allen Global, Inc. (incorporated by reference to Exhibit 3(e) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)</u>                                                                                                                                                                    |
| 3 (f)   | <u>By-laws of Ethan Allen Global, Inc. (incorporated by reference to Exhibit 3(f) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)</u>                                                                                                                                                                                         |
| 3 (g)   | <u>Restated Certificate of Incorporation of Ethan Allen Inc. (now known as, Ethan Allen Retail, Inc.) (incorporated by reference to Exhibit 3(g) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)</u>                                                                                                                          |
| 3 (g)-1 |                                                                                                                                                                                                                                                                                                                                                                                             |

Certificate of Amendment of Restated Certificate of Incorporation of Ethan Allen Inc. (now known as Ethan Allen Retail, Inc.) as of June 29, 2005 (incorporated by reference to Exhibit 3(g)-1 to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)

3 (h) Amended and Restated By-laws of Ethan Allen Inc. (now known as Ethan Allen Retail, Inc.) (incorporated by reference to Exhibit 3(h) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)

3 (i) Certificate of Incorporation of Ethan Allen Manufacturing Corporation (now known as Ethan Allen Operations, Inc.) (incorporated by reference to Exhibit 3(i) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)

3 (i)-1 Certificate of Amendment of Certificate of Incorporation of Ethan Allen Manufacturing Corporation (now known as, Ethan Allen Operations, Inc.) as of June 29, 2005 (incorporated by reference to Exhibit 3(i)-1 to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)

3 (j) By-laws of Ethan Allen Manufacturing Corporation (now known as, Ethan Allen Operations, Inc.) (incorporated by reference to Exhibit 3(j) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)

3 (k) Certificate of Formation of Ethan Allen Realty, LLC (incorporated by reference to Exhibit 3(k) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

- 3 (l) Limited Liability Company Operating Agreement of Ethan Allen Realty, LLC (incorporated by reference to Exhibit 3(l) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)
- 3 (l)-1 Amendment No. 1 to Operating Agreement of Ethan Allen Realty, LLC as of June 30, 2005 (incorporated by reference to Exhibit 3(l)-1 to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)
- 3 (m) Certificate of Incorporation of Lake Avenue Associates, Inc. (incorporated by reference to Exhibit 3(m) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)
- 3 (n) By-laws of Lake Avenue Associates, Inc. (incorporated by reference to Exhibit 3(n) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)
- 3 (o) Certificate of Incorporation of Manor House, Inc. (incorporated by reference to Exhibit 3(o) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)
- 3 (p) Restated By-laws of Manor House, Inc. (incorporated by reference to Exhibit 3(p) to the Registration Statement on Form S-4 of Ethan Allen Global, Inc. filed with the SEC on February 3, 2006)
- 10 (a) Restated Directors Indemnification Agreement dated March 1993, among the Company and Ethan Allen and their Directors (incorporated by reference to Exhibit 10(c) to the Registration Statement on Form S-1 of the Company filed with the SEC on March 16, 1993)
- 10 (b) The Ethan Allen Retirement Savings Plan as Amended and Restated, effective January 1, 2006 (incorporated by reference to Exhibit 10(b)-7 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on November 5, 2007) †
- 10 (c) Sales Finance Agreement, dated June 25, 1999, between the Company and MBNA America Bank, N.A. (incorporated by reference to Exhibit 10(j) to the Annual Report on Form 10-K of the Company filed with the SEC on September 13, 2000)
- 10 (d) Second Amended and Restated Private Label Consumer Credit Card Program Agreement, dated as of July 23, 2007, by and between Ethan Allen Global, Inc., Ethan Allen Retail, Inc. and GE Money Bank (incorporated by reference to Exhibit 10(e)-3 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on November 5, 2007)(confidential treatment granted under Rule 24b-2 as to certain portions which are omitted and filed separately with the SEC)
- 10 (d)-1 First Amendment to Second Amended and Restated Private Label Consumer Credit Card Program Agreement, dated as of July 25, 2008, by and between Ethan Allen Global, Inc., Ethan Allen Retail, Inc. and GE Money Bank (incorporated by reference as Exhibit 10(e)-1 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on May 10, 2010)



- 10 Second Amendment to Second Amended and Restated Private Label Consumer Credit Card Program  
(d)-2 Agreement, dated as of February 16, 2010, by and between Ethan Allen Global, Inc., Ethan Allen Retail, Inc. and GE Money Bank (incorporated by reference as Exhibit 10(e)-2 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on May 10, 2010) (confidential treatment granted under Rule 24b-2 as to certain portions which are omitted and filed separately with the SEC)

- Third Amendment to Second Amended and Restated Private Label Consumer Credit Card Program  
10 Agreement, dated as of June 30, 2011, by and between Ethan Allen Global, Inc., Ethan Allen Retail, Inc. and  
(d)-3 GE Money Bank (incorporated by reference to Exhibit 10(e)-3 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on November 3, 2010) (confidential treatment under Rule 24b-2 requested as to certain portions which are omitted and filed separately with the SEC)

- Fourth Amendment to Second Amended and Restated Private Label Consumer Credit Card Program  
10 Agreement dated as of January 1, 2014, by and between Ethan Allen Global, Inc., Ethan Allen Retail, Inc., and  
(d)-4 GE Capital Retail Bank (incorporated by reference to Exhibit 10(d)-4 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on January 31, 2014) (confidential treatment requested under Rule 24b-2 as to certain portions which are omitted and filed separately with the SEC)

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

10 Fifth Amendment to Second Amended and Restated Private Label Consumer Credit Card Program Agreement  
(d)-5 effective as of July 1, 2015, by and between Ethan Allen Global, Inc., Ethan Allen Retail, Inc., and Synchrony  
Bank (incorporated by reference to Exhibit 10.(D)-5 to the Annual Report on Form 10-K of the Company filed  
with the SEC on August 12, 2015) (confidential treatment requested under Rule 24b-2 as to certain portions  
which are omitted and filed separately with the SEC)

10 (e) Employment Agreement between the Company and M. Farooq Kathwari dated October 1, 2015 (incorporated  
by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on October 2,  
2015). †

10 Form of Performance-Based Stock Unit Agreement (incorporated by reference to Exhibit 10.2 to the  
(e)-1 Company's Current Report on Form 8-K filed with the SEC on October 2, 2015) †

10 Change in Control Severance Plan (incorporated by reference to Exhibit 10.3 to the Company's Current Report  
(e)-2 on Form 8-K filed with the SEC on October 2, 2015) †

10 Credit Agreement, dated as of May 29, 2009, among Ethan Allen Global, Inc., Ethan Allen Interiors Inc., J.P.  
(f)-1 Morgan Chase Bank, N.A., and Capital One Leverage Finance Corp (confidential treatment requested as to  
certain portions (Incorporated by reference to Exhibit 10(g)-2 to the Annual Report on Form 10-K of the  
Company filed with the SEC on August 24, 2009)

10 Amendment No. 1, dated as of October 23, 2009 to the Credit Agreement dated May 29, 2009, among Ethan  
(f)-2 Allen Global, Inc., Ethan Allen Interiors Inc., J.P.Morgan Chase Bank, N.A., and the lenders thereunder  
(incorporated by reference to Exhibit 10(g)-3 to the Quarterly Report on Form 10-Q of the Company filed with  
the SEC on November 9, 2009).

10 Amendment No. 2, dated as of March 25, 2011, to the Credit Agreement dated May 29, 2009, among Ethan  
(f)-3 Allen Global, Inc., Ethan Allen Interiors Inc., J.P.Morgan Chase Bank, N.A., and Wells Fargo Bank, National  
Association (incorporated by reference to Exhibit 10(g)-3 to the Quarterly Report on Form 10-Q of the  
Company filed with the SEC on May 5, 2011)

10 Amended and Restated Credit Agreement, dated October 21, 2014, among Ethan Allen Global, Inc., Ethan  
(f)-4 Allen Interiors Inc., J.P. Morgan Chase Bank, N.A., and Capital One, National Association (incorporated by  
reference to Exhibit 10.1 to the Current Report on Form 8-K of the Company filed with the SEC on October  
22, 2014)

10 Amendment No. 2 Dated as of September 10, 2015 to Amended and restated credit agreement dated as of  
(f)-5 October 21, 2014 among Ethan Allen Global, Inc., and J.P. Morgan Chase Bank, N.A. as Administrative Agent  
and Syndication Agent, and Capital One, National Association as Documentation Agent dated as of October  
21, 2014 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 8-K filed with  
the SEC on September 11, 2015)

10 Amendment No. 3, dated as of January 22, 2016, to the Amended and Restated Credit Agreement dated as of  
(f)-6 October 21, 2014 among Ethan Allen Global, Inc., Ethan Allen Interiors Inc., J.P.Morgan Chase Bank, N.A.

and Capital One, National Association (incorporated by reference to the Company's Quarterly Report on Form 10-Q filed with the SEC on January 27, 2016).

- 10 (g) Amended and Restated 1992 Stock Option Plan (incorporated by reference to Exhibit 10(f) to the Current Report on Form 8-K of the Company filed with the SEC on November 19, 2007). †
- 10 Form of Option Agreement for Grants to Independent Directors (incorporated by reference to Exhibit 10(h)-4  
(g)-1 to the Annual Report on Form 10-K of the Company filed with the SEC on September 13, 2005). †
- 10 Form of Option Agreement for Grants to Employees (incorporated by reference to Exhibit 10(h)-5 to the  
(g)-2 Annual Report on Form 10-K of the Company filed with the SEC on September 13, 2005). †
- 10 Form of Restricted Stock Agreement for Executives (incorporated by reference to Exhibit 10(f)-1 to the  
(g)-3 Current Report on Form 8-K of the Company filed with the SEC on November 19, 2007). †

## ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES

- 10 (g)-4 Form of Restricted Stock Agreement for Directors (incorporated by reference to Exhibit 10(f)-2 to the Current Report on Form 8-K of the Company filed with the SEC on November 19, 2007) †
- 10 (g)-5 Form of performance condition option agreement for employees (incorporated by reference to Exhibit 10(g)-5 to the Quarterly Report on Form 10-Q of the Company filed with the SEC on May 1, 2014) †
- 21 List of wholly-owned subsidiaries of the Company (incorporated by reference to Exhibit 21 to the Annual Report on Form 10-K of the Company filed with the SEC on August 2, 2017)
- 23 Consent of KPMG LLP
- 31.1 Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \* 32.1 Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \* 32.2 Certification of Principal Financial Officer 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
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase
- 101.DEF XBRL Taxonomy Extension Definition Linkbase
- 101.LAB XBRL Taxonomy Extension Labels Linkbase
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase

\* Furnished herewith.

† Management contract or compensatory plan, contract or arrangement.

### **Item 16. Form 10-K Summary**

None.

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**ETHAN ALLEN INTERIORS INC. AND SUBSIDIARIES**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

ETHAN ALLEN INTERIORS INC.

(Registrant)

DATE: August 2, 2018

By /s/ M. Farooq Kathwari  
(M. Farooq Kathwari)

Chairman, President and Chief Executive Officer

(Principal Executive Officer)

DATE: August 2, 2018

By /s/ Corey Whitely  
(Corey Whitely)

Executive Vice President, Administration, Chief Financial  
Officer and Treasurer

(Principal Financial Officer)

KNOW ALL MEN BY THESE PRESENTS, that each individual whose signature appears below hereby constitutes and appoints M. Farooq Kathwari and Corey Whitely, and each of them individually, his or her true and lawful agent, proxy and attorney-in-fact, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to (i) act on, sign and file with the Securities and Exchange Commission any and all amendments to this Report together with all schedules and exhibits thereto, (ii) act on, sign and file with the Securities and Exchange Commission any and all exhibits to this Report and any and all exhibits and schedules thereto, (iii) act on, sign and file any and all such certificates, notices, communications, reports, instruments, agreements and other documents as may be necessary or appropriate in connection therewith and (iv) take any and all such actions which may be necessary or appropriate in connection therewith, granting unto such agents, proxies and attorneys-in-fact, and each of them individually, full power and authority to do and perform each and every act and thing necessary or appropriate to be done, as fully for all intents and purposes as he or she might or could do in person, and hereby approving, ratifying and confirming all that such agents, proxies and attorneys-in-fact, any of them or any of his, her or their substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

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Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

/s/ M. Farooq Kathwari      Chairman, President and Chief Executive Officer  
(M. Farooq Kathwari)      (Principal Executive Officer)

/s/ Corey Whitely      Executive Vice President, Administration,  
Chief Financial Officer and Treasurer  
(Corey Whitely)      (Principal Financial Officer)

/s/ John S. Bedford      Vice President, Corporate Controller  
(John S. Bedford)      (Principal Accounting Officer)

/s/ James B. Carlson      Director  
(James B. Carlson)

/s/ John J. Dooner Jr.      Director  
(John J. Dooner Jr.)

/s/ Domenick J. Esposito      Director  
(Domenick J. Esposito)

/s/ Mary Garrett      Director  
(Mary Garrett)

/s/ James W. Schmotter      Director  
(James W. Schmotter)

/s/ Tara I. Stacom      Director  
(Tara I. Stacom)

Date: August 2, 2018