

Leatt Corp  
Form 10-Q  
August 12, 2016

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

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended: **June 30, 2016**

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

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

Commission File No. **000-54693**

**LEATT CORPORATION**

*(Exact name of registrant as specified in its charter)*

**Nevada**

*(State or other jurisdiction of incorporation or  
organization)*

**20-2819367**

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

**50 Kiepersol Drive, Atlas Gardens, Contermanskloof Road,  
Durbanville, Western Cape, South Africa, 7441**

*(Address of principal executive offices)*

**+(27) 21-557-7257**

*(Registrant's telephone number, including area code)*

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§

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232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

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

Large accelerated filer [ ] Accelerated filer [ ]  
Non-accelerated filer [ ] Smaller reporting company [X]

(Do not check if a smaller reporting company)

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

The number of shares outstanding of each of the issuer's classes of common stock, as of August 4, 2016 is as follows:

<u>Class of Securities</u>	<u>Shares Outstanding</u>
<b><u>Common Stock, \$0.001 par value</u></b>	<b><u>5,270,592</u></b>

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LEATT CORPORATION

*Quarterly Report on Form 10-Q  
Three Months and Six Months Ended June 30, 2016*

TABLE OF CONTENTS

<u>PART I</u>	<u>1</u>
<u>FINANCIAL INFORMATION</u>	
<b><u>ITEM 1. FINANCIAL STATEMENTS.</u></b>	<u>1</u>
<b><u>ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.</u></b>	<u>11</u>
<b><u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.</u></b>	<u>21</u>
<b><u>ITEM 4. CONTROLS AND PROCEDURES.</u></b>	<u>21</u>
<u>PART II</u>	<u>21</u>
<u>OTHER INFORMATION</u>	
<b><u>ITEM 1. LEGAL PROCEEDINGS.</u></b>	<u>21</u>
<b><u>ITEM 1A. RISK FACTORS.</u></b>	<u>22</u>
<b><u>ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.</u></b>	<u>22</u>
<b><u>ITEM 3. DEFAULTS UPON SENIOR SECURITIES.</u></b>	<u>22</u>
<b><u>ITEM 4. MINE SAFETY DISCLOSURES.</u></b>	<u>22</u>
<b><u>ITEM 5. OTHER INFORMATION.</u></b>	<u>22</u>
<b><u>ITEM 6. EXHIBITS.</u></b>	<u>23</u>

PART I  
FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

LEATT CORPORATION  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2016 AND 2015

	<b>Page(s)</b>
Financial Statements	
<u>Consolidated Balance Sheets</u>	<u>2</u>
<u>Consolidated Statements of Operations and</u>	<u>3</u>
<u>Comprehensive Income (Loss)</u>	
<u>Consolidated Statement of Changes in Stockholders'</u>	<u>4</u>
<u>Equity</u>	
<u>Consolidated Statements of Cash Flows</u>	<u>5</u>
<u>Notes to Consolidated Financial Statements</u>	<u>6 - 7</u>

**LEATT CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

**ASSETS**

	<b>June 30, 2016</b>	<b>December 31, 2015</b>
	<b>Unaudited</b>	<b>Audited</b>
<b>Current Assets</b>		
Cash and cash equivalents	\$ 1,000,759	\$ 1,054,750
Short-term investments	58,184	58,172
Accounts receivable	2,078,095	2,901,699
Inventory	3,963,139	4,241,140
Payments in advance	606,536	208,030
Prepaid expenses and other current assets	707,660	1,070,774
Total current assets	8,414,373	9,534,565
<b>Property and equipment, net</b>		
Property and equipment, net	1,170,527	1,313,325
Deferred tax asset	115,000	115,000
<b>Other Assets</b>		
Other receivables	30,000	90,000
Deposits	16,713	16,493
Intangible assets	62,851	61,273
Total other assets	109,564	167,766
<b>Total Assets</b>	<b>\$ 9,809,464</b>	<b>\$ 11,130,656</b>

**LIABILITIES AND STOCKHOLDERS' EQUITY**

<b>Current Liabilities</b>		
Accounts payable and accrued expenses	\$ 1,505,751	\$ 2,560,980
Income taxes payable	251,349	384,950
Short term loan, net of finance charges	271,625	658,639
Total current liabilities	2,028,725	3,604,569
Deferred tax liabilities	73,000	73,000
<b>Commitments and contingencies</b>		
<b>Stockholders' Equity</b>		
Preferred stock, \$.001 par value, 1,120,000 shares authorized, 120,000 shares issued and outstanding	3,000	3,000
Common stock, \$.001 par value, 28,000,000 shares authorized, 5,270,592 and 5,231,823 shares issued and outstanding	130,053	130,040
Additional paid - in capital	7,467,978	7,346,782
Accumulated other comprehensive loss	(678,113)	(710,032)
Retained earnings	784,821	683,297
Total stockholders' equity	7,707,739	7,453,087
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 9,809,464</b>	<b>\$ 11,130,656</b>

See accompanying notes to consolidated financial statements

**LEATT CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)**

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2016	2015	2016	2015
	Unaudited	Unaudited	Unaudited	Unaudited
Revenues	\$ 3,693,915	\$ 5,193,056	\$ 8,521,407	\$ 9,214,511
Cost of Revenues	1,710,012	2,361,827	4,023,669	4,206,022
Gross Profit	1,983,903	2,831,229	4,497,738	5,008,489
Product Royalty Income	39,649	20,668	53,531	72,201
<b>Operating Expenses</b>				
Salaries and wages	523,912	542,467	1,205,214	1,148,645
Commissions and consulting expenses	133,921	151,468	299,992	337,376
Professional fees	70,659	246,392	252,318	461,165
Advertising and marketing	352,801	363,313	714,394	624,755
Office rent and expenses	62,962	62,543	127,152	123,051
Research and development costs	338,244	293,666	681,059	586,383
Bad debt expense (recovery)	(25,384)	19,461	(22,557)	19,461
General and administrative expenses	514,852	489,116	961,798	914,332
Depreciation	106,481	91,473	210,998	184,276
Total operating expenses	2,078,448	2,259,899	4,430,368	4,399,444
Income (Loss) from Operations	(54,896)	591,998	120,901	681,246
<b>Other Income</b>				
Interest and other income, net	70,750	7,539	68,809	7,981
Total other income	70,750	7,539	68,809	7,981
Income Before Income Taxes	15,854	599,537	189,710	689,227
Income Taxes	27,310	175,600	88,186	211,185
Net Income (Loss) Available to Common Shareholders	\$ (11,456)	\$ 423,937	\$ 101,524	\$ 478,042
<b>Net Income (Loss) per Common Share</b>				
Basic	\$ -	\$ 0.08	\$ 0.02	\$ 0.09
Diluted	\$ -	\$ 0.08	\$ 0.02	\$ 0.09
<b>Weighted Average Number of Common Shares Outstanding</b>				
Basic	5,270,592	5,201,663	5,251,932	5,201,143
Diluted	5,508,380	5,476,017	5,489,720	5,475,497
<b>Comprehensive Income (Loss)</b>				

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Net Income (Loss)	\$	(11,456)	\$	423,937	\$	101,524	\$	478,042
Other comprehensive income (loss), net of \$0 and \$0 deferred income taxes in 2016 and 2015								
Foreign currency translation		8,870		(40,422)		31,919		(86,891)
Total Comprehensive Income (Loss)	\$	(2,586)	\$	383,515	\$	133,443	\$	391,151

See accompanying notes to consolidated financial statements



**LEATT CORPORATION**  
**CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY**  
**AS OF AND FOR THE SIX MONTHS ENDED JUNE 30, 2016**

	Preferred Stock A Shares	Amount	Common Stock Shares	Amount	Additional Paid - In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Total
Balance, January 1, 2016	120,000	\$ 3,000	5,231,823	\$ 130,040	\$ 7,346,782	\$ (710,032)	\$ 683,297	\$ 7,453,087
Compensation cost recognized in connection with stock options	-	-	-	-	155,742	-	-	155,742
Exercise of stock options	-	-	39,000	39	38,961	-	-	39,000
Options exercised on a cashless basis	-	-	26,220	-	-	-	-	-
Common shares returned to authorized and unissued status	-	-	(26,451)	(26)	(73,507)	-	-	(73,533)
Net income	-	-	-	-	-	-	101,524	101,524
Foreign currency translation adjustment	-	-	-	-	-	31,919	-	31,919
Balance, June 30, 2016	120,000	\$ 3,000	5,270,592	\$ 130,053	\$ 7,467,978	\$ (678,113)	\$ 784,821	\$ 7,707,739

See accompanying notes to consolidated financial statements

**LEATT CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE SIX MONTHS ENDED JUNE 30, 2016 AND 2015**

	2016	2015
Cash flows from operating activities		
Net income	\$ 101,524	\$ 478,042
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	210,998	184,276
Deferred income taxes	-	(276)
Stock-based compensation	155,742	1,478
Return of common stock	(73,533)	-
Bad debts	(22,557)	-
Inventory reserve	13,180	164,543
Gain on sale of property and equipment	-	(6,067)
(Increase) decrease in:		
Accounts receivable	846,161	2,046,798
Inventory	264,821	(209,497)
Payments in advance	(398,506)	(105,148)
Prepaid expenses and other current assets	363,114	224,903
Income tax refunds receivable	-	25,000
Other receivables	60,000	60,000
Deposits	(220)	287
Decrease in:		
Accounts payable and accrued expenses	(1,055,229)	(1,903,575)
Income taxes payable	(133,601)	(11,000)
Net cash provided by operating activities	331,894	949,764
Cash flows from investing activities		
Capital expenditures	(52,629)	(65,872)
Proceeds from sale of property and equipment	-	12,200
Increase in short-term investments, net	(12)	(8)
Net cash used in investing activities	(52,641)	(53,680)
Cash flows from financing activities		
Proceeds from exercise of stock options	39,000	31,200
Repayments of short-term loan, net	(387,014)	(365,757)
Net cash used in financing activities	(348,014)	(334,557)
Effect of exchange rates on cash and cash equivalents	14,770	(67,271)
Net increase (decrease) in cash and cash equivalents	(53,991)	494,256
Cash and cash equivalents - beginning	1,054,750	724,707
Cash and cash equivalents - ending	\$ 1,000,759	\$ 1,218,963
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	\$ 6,920	\$ 6,202
Cash paid for income taxes	\$ 221,787	\$ 222,185

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Other noncash investing and financing activities			
Common stock issued for services	\$	155,742	\$ 1,478
Common stock returned to authorized and unissued status	\$	(73,533)	\$ -

See accompanying notes to consolidated financial statements

- 7 -

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**LEATT CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**Note 1 - Basis of presentation**

The consolidated balance sheet as of December 31, 2015 was audited and appears in the Form 10-K filed by the Company with the Securities and Exchange Commission on March 18, 2016. The consolidated balance sheet as of June 30, 2016 and the consolidated statements of operations and comprehensive income (loss) for the three and six months ended June 30, 2016 and 2015, changes in stockholders' equity for the six months ended June 30, 2016, cash flows for the six months ended June 30, 2016 and 2015, and the related information contained in these notes have been prepared by management without audit. In the opinion of management, all adjustments (which include only normal recurring items) necessary to present fairly the financial position, results of operations and cash flows in conformity with generally accepted accounting principles as of June 30, 2016 and for all periods presented have been made. Interim operating results are not necessarily indicative of operating results for a full year.

Certain information and note disclosures normally included in the Company's annual financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. While management of the Company believes that the disclosures presented are adequate to make the information not misleading, it is suggested that these condensed consolidated financial statements be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2015 as filed with the Securities and Exchange Commission in the Company's Form 10-K.

**Note 2 - Inventory**

Inventory is stated at the lower of cost or market. Cost is determined using the first-in first-out (FIFO) method. Inventory consists primarily of finished goods. Shipping and handling costs are included in the cost of inventory. In assessing the inventory value, the Company must make estimates and judgments regarding reserves required for product obsolescence, aging of inventory and other issues potentially affecting the saleable condition of products. In performing such evaluations, the Company utilizes historical experience as well as current market information. The reserve for obsolescence as of the six months ended June 30, 2016 and 2015 was \$173,695 and \$322,355, respectively.

**Note 3 - Intangible Assets**

The Company's intangible assets consist of acquired patents with an indefinite useful life and are thus not amortized. Intangible assets are carried at cost less impairment. Amortization expense for the six months ended June 30, 2016 was zero. There was no impairment of intangible assets at June 30, 2016.

**Note 4 - Short-term Loan**

The Company carries two product liability insurance policies; one with a U.S. insurance carrier and a second with a South African insurance carrier. The Company finances payment of its short-term insurance premiums over the period of coverage, which is generally twelve months. The U.S. short-term loan is payable in monthly installments of \$71,952 over an 11-month period at an APR of 2.897% and the South African short-term loan is payable in monthly installments of \$1,561 over a 10-month period at a flat interest rate of 3.90%.

The Company also carries directors and officers' liability insurance. The Company finances payment of its short-term insurance premiums over the period of coverage, which is generally twelve months. The short-term loan is payable in eleven payments of \$5,375 at a 3.397% annual interest rate.

**Note 5- Income Taxes**

The Company uses the asset and liability approach to account for income taxes. Deferred tax assets and liabilities are determined based on the differences between the financial statement carrying amounts and the income tax basis of assets and liabilities. A valuation allowance is applied against any net deferred tax asset if, based on available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The provision for income taxes included taxes currently payable, if any, plus the net change during the period in deferred tax assets and liabilities recorded by the Company.

The Company applies the provisions of FASB ASC Topic 740-10, Accounting for Uncertainty in Income Taxes ( Standard ), which provides that the tax effects from an uncertain tax position can be recognized in the consolidated financial statements only if the position is more likely than not of being sustained upon an examination by tax authorities. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, the standard provides guidance on derecognition, classification, interest and penalties; accounting in interim periods, disclosure and transition, and any amounts when incurred would be recorded under these provisions.

The Company's practice is to recognize interest and/or penalties related to income tax matters in income tax expense. As of June 30, 2016 the Company has no unrecognized tax benefits.

#### Note 6 - Net Income Per Share of Common Stock

Basic net income per common share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted average number of common stock shares and dilutive potential common shares outstanding during the period. For the six months ended June 30, 2016, the Company had 627,000 potential common shares, consisting of 120,000 preferred shares and options to purchase 507,000 shares outstanding. Of the total options to purchase common shares, 323,000 were antidilutive and were therefore not included in diluted net income per share.

#### Note 7 Common Stock

During the six months ended June 30, 2016, 323,000 stock options were granted at an exercise price of \$2.60 per share, exercisable over a 5-year period. The fair value of the stock options granted was estimated at the date of grant using the Black Sholes option-pricing model. Based on the list of assumptions presented below, the fair value of the options granted during the six months ended June 30, 2016, was \$1.80.

Expected term in years	5 years
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Risk-free interest rate	2.20%
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Expected volatility	0.88%
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Expected dividend yield	0.00%
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The expected volatility was determined with reference to the historical volatility of the Company's stock. The Company uses historical data to estimate option exercise and employee termination within the valuation model. The expected term of options granted represents the period of time that the options granted are expected to be outstanding. The risk-free interest rate for periods within the contractual life of the option is based on the U.S. Treasury rate in effect at the time of grant.

Stock-based compensation expense related to vested stock options granted during the six months ended June 30, 2016 was \$155,440. As of June 30, 2016, there was \$426,960 of unrecognized compensation costs related to unvested stock options, which is expected to be recognized over a 3-year vesting period.

In addition, on April 7, 2016, the Company issued 26,220 shares of common stock to employees who exercised employee stock options in a cashless exercise; and on March 29, 2016 an employee exercised stock options for the Company to issue 39,000 shares for \$39,000. On May 24, 2016, the Company also cancelled and returned 26,451 shares of common stock, granted to a former employee, to authorized and unissued status in settlement of a legal matter. The fair value of the shares as of the date of cancellation was \$73,533 and is included in other income for the three and six months ended June 30, 2016.

#### Note 8 Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers*, (ASU 2014-09). ASU 2014-09, as amended, outlines a new, single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. This new revenue recognition model provides a five-step analysis in determining when and how revenue is recognized. The new model will require an entity to recognize revenue when it transfers promised goods or services to customers in an amount that reflects what it expects in exchange for the goods

or services. On August 12, 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*". The amendments in this update defers the effective date of Update 2014-09 for all entities by one year. The ASU, as amended, is effective for the first interim period within an annual period beginning after December 15, 2017, and early adoption is not permitted. The Company is evaluating the provisions of this update and has not determined the impact that its adoption will have on the Company's financial position or results of operations.

In July 2015, the FASB issued ASU 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory*, which applies to inventory that is measured using first-in, first-out (FIFO) or average cost. This ASU simplifies the subsequent measurement of inventories by replacing the lower of cost or market test with a lower of cost or net realizable value test. The ASU is effective for annual periods beginning after December 15, 2016. Early adoption is permitted. The Company does not expect the adoption of this ASU to have a material effect on the consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*." This ASU requires that deferred tax assets and liabilities be classified as non-current on the balance sheet rather than being separated into current and non-current. This ASU is effective for annual and interim periods within those years, beginning after December 15, 2016. Early adoption is permitted. The Company elected to retrospectively adopt this accounting standard in the beginning of the first quarter of fiscal 2016 and as a result, prior periods in the consolidated financial statements were adjusted.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. This ASU is a comprehensive new lease standard that amends various aspects of existing accounting guidance for leases. The core principle of this ASU will require lessees to present the assets and liabilities that arise from leases on their balance sheets. The ASU is effective for public companies for annual and interim reporting periods beginning after December 15, 2018. Early adoption is permitted. The Company is evaluating the new standard to determine the impact on the Company's consolidated financial statements.

In March 2016, the FASB issued Accounting Standards Update No 2016-09 *Improvements to Employee Share-Based Payment Accounting* ("ASC 2016-09"). ASC 2016-09 will change certain aspects of accounting for share-based payments to employees. The new guidance will require all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It also will allow an employer to repurchase more of an employee's shares than it can today for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. The ASU is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company is evaluating the new standard to determine the impact on the Company's consolidated financial statements.

The Company does not believe there are any other recent accounting pronouncements that would have a material impact on its financial position or results of operations.

#### **Note 9 - Litigation**

In the ordinary course of business, the Company is involved in various legal proceedings involving product liability and personal injury and intellectual property litigation. The Company is insured against loss for certain of these matters. The Company will record contingent liabilities resulting from asserted and unasserted claims against it when it is probable that the liability has been incurred and the amount of the loss is reasonably estimable. The Company will disclose contingent liabilities when there is a reasonable possibility that the ultimate loss will exceed the recorded liability. While the outcome of currently pending litigation is not yet determinable, the ultimate exposure with respect to these matters cannot be ascertained. However, based on the information currently available to the Company, the Company does not expect that any liabilities or costs that might be incurred to resolve these matters will have a material adverse effect on the financial condition, results of operations, liquidity or cash flows of the Company.

#### **Note 10 Subsequent Events**

The company has evaluated all subsequent events through the date the financial statements were released.



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

### Special Note Regarding Forward Looking Statements

This report contains forward-looking statements that are contained principally in the sections entitled Our Business, Risk Factors, and Management's Discussion and Analysis of Financial Condition and Results of Operations. These statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. These risks and uncertainties include, but are not limited to, the factors described in the section captioned Risk Factors above. In some cases, you can identify forward-looking statements by terms such as anticipates, believes, could, estimates, expects, intends, may, plans, projects, should, would and similar expressions intended to identify forward-looking statements. Forward-looking statements reflect our current views with respect to future events and are based on assumptions and subject to risks and uncertainties. Given these uncertainties, you should not place undue reliance on these forward-looking statements. These forward-looking statements include, among other things, statements relating to:

- our expectations regarding growth in the motor sports market;
- our expectation regarding increasing demand for protective equipment used in the motor sports market;
- our belief that we will be able to effectively compete with our competitors and increase our market share;
- our expectations with respect to increased revenue growth and our ability to achieve profitability resulting from increases in our production volumes; and
- our future business development, results of operations and financial condition.

Also, forward-looking statements represent our estimates and assumptions only as of the date of this quarterly report. You should read this quarterly report and the documents that we reference and filed as exhibits to the quarterly report completely and with the understanding that our actual future results may be materially different from what we expect. Except as required by law, we assume no obligation to update any forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in any forward-looking statements, even if new information becomes available in the future.

### Use of Certain Defined Terms

Except as otherwise indicated by the context, references in this quarterly report to:

- Leatt, we, us, our, the Registrant or the Company are to the combined business of Leatt Corporation, corporation, its South African branch, Leatt SA, and its direct, wholly-owned subsidiaries, Two Eleven, Leatt New Zealand and Three Eleven;
- Leatt SA are to the Company's branch office known as Leatt Corporation (Incorporated in the State of Nevada) incorporated under the laws of South Africa with registration number: 2007/032780/10;
- Leatt USA are to Leatt USA, LLC, a Nevada Limited Liability Company;
- Leatt New Zealand are to Leatt New Zealand Limited, a New Zealand Company;
- NZD are to the legal currency of New Zealand. For all NZD amounts reported, the dollar amount has been calculated on the basis that \$1=NZD1.4093 for its June 30, 2016 balance sheet.
- PRC, and China are to the People's Republic of China;
- Two Eleven refers to Two Eleven Distribution, LLC, a California limited liability company;
- Three Eleven are to Three Eleven Distribution (Pty) Limited, a South African Company;
- Securities Act are to the Securities Act of 1933, as amended, and to Exchange Act are to Securities Exchange Act of 1934, as amended;
- South Africa are to the Republic of South Africa;
- U.S. dollar, \$ and US\$ are to the legal currency of the United States.

- Xceed Holdings refers to Xceed Holdings cc., a close corporation incorporated under the laws of South Africa, and wholly-owned by The Leatt Family Trust, of which Dr. Christopher J. Leatt, the Company's chairman, is a Trustee and Beneficiary; and
- ZAR refers to the South African Rand, the legal currency of South Africa. For all ZAR amounts reported, the dollar amount has been calculated on the basis that \$1 = ZAR15.0113 for its June 30, 2016 balance sheet.

### **Overview of our Business**

Leatt designs, develops, markets and distributes personal protective equipment for participants in all forms of motor sports and leisure activities, including riders of motorcycles, bicycles, snowmobiles and ATVs, as well as racing car drivers. The Company sells its products to customers worldwide through a global network of distributors and retailers. Leatt also acts as the original equipment manufacturer for neck braces sold by other international brands.

The Company's flagship products are based on the Leatt-Brace® system, a patented injection molded neck protection system owned by Xceed Holdings, designed to prevent potentially devastating injuries to the cervical spine and neck. The Company has the exclusive global manufacturing, distribution, sale and use rights to the Leatt-Brace®, pursuant to a license agreement between the Company and Xceed Holdings, a company owned and controlled by the Company's Chairman and founder, Dr. Christopher Leatt. The Company also has the right to use apparatus embodying, employing and containing the Leatt-Brace® technology and has designed, developed, marketed and distributed other personal protective equipment using this technology, as well as its own developed technology, including the Company's expanding range of body protection and helmet products which it markets under the Leatt Protection Range brand.

The Company's research and development efforts are conducted at its research facilities, located at its executive headquarters in Cape Town, South Africa. The Company employs 4 full-time employees who are dedicated exclusively to research, development, and testing. The Company also utilizes consultants, academic institutions and engineering companies as independent contractors or consultants, from time to time, to assist it with its research and development efforts. Leatt products have been tested and reviewed internally and by external bodies. All Leatt products are compliant with applicable European Union directives, or CE certified, where appropriate. Certain products, such as the MRX PRO Head and Neck Restraint System, have been certified by SFI Foundation (USA) and the Moto GPX was tested by BMW Motorrad (Germany) and reviewed by KTM (Austria). The Company is also in discussions with governing and racing bodies, such as the Fédération Internationale de l'Automobile (FIA), the Fédération Internationale de Motocyclisme (FIM) and the National Association for Stock Car Auto Racing (NASCAR), to have the Leatt-Brace® accredited by these bodies.

Our products are manufactured in China under outsource manufacturing arrangements with third-party manufacturers located there. The Company utilizes outside consultants and its own employees to ensure the quality of its products through regular on-site product inspections. Products purchased through international sales are usually shipped directly from our manufacturers' warehouses or points of dispatch to customers or their import agents.

Leatt earns revenues through the sale of its products through approximately 60 distributors worldwide, who in turn sell its products to retailers. Leatt distributors are required to follow certain standard business terms and guidelines for the sale and distribution of Leatt products. Two Eleven and Leatt SA directly distribute Leatt products to retailers in the United States and South Africa, respectively.

### **Principal Factors Affecting Our Financial Performance**

We believe that the following factors will continue to affect our financial performance:

- ***Global Economic Fragility and Currency Fluctuations*** A portion of our revenues are earned in international markets and the ongoing turmoil in the global economy, especially in Europe, including the recent decision of United Kingdom (UK) voters to leave the European Union (EU), may have an impact on our business and our financial condition. This economic turmoil has led to continued currency weakness in our international markets against a strengthening U.S. Dollar, resulting in declining revenues from sales in those markets. We may face more challenges from currency moves as the UK moves forward with plans to exit the EU and if economic conditions do not otherwise improve. These economic conditions impact levels of consumer spending in international markets, which have declined and may remain so for the foreseeable future. If demand for our products fluctuates as a result of these economic conditions or otherwise, our revenue and gross margin will continue to be harmed. Management continues to monitor currency fluctuations globally and evaluate marketing and sales strategies accordingly.
- ***Fuel Prices*** Significant fluctuations in fuel prices could have both a positive and negative effect on our business and operations. A significant portion of our revenue is derived from international sales and significant fluctuations in world fuel prices could significantly increase the price of shipping or transporting our products which we may not be able to pass on to our customers. On the other hand, fluctuations in fuel prices lead to higher commuter costs which may encourage the increased use of motorcycles and bicycles as alternative modes of transportation and lead to an increase in the market for our protection products.
- ***Product Liability Litigation*** We face an inherent business risk of exposure to product liability claims arising from the claimed failure of our products to help prevent the types of personal injury or death against which they are designed to help protect. Therefore, we have acquired very costly product liability insurance worldwide. We have not experienced any material uninsured losses due to product liability claims, but it is possible that we could experience material losses in the future. After a two-week trial in the United States District Court for the Northern District of Ohio (Eastern) ending on April 17, 2014, a federal jury returned a defense verdict for the Company in the first Leatt-Brace® product liability lawsuit to be tried in the United States. The plaintiffs in that case had alleged that defective product design and failure to warn had caused a

then fifteen-year-old motocross rider, to suffer multiple mid-thoracic spine fractures, causing immediate and permanent paraplegia, when he crashed at a relatively low speed on February 13, 2011. When the accident occurred, he was wearing a helmet and other safety gear from several different companies, including the Company's acclaimed Leatt-Brace®. The Company produced evidence at trial showing that his thoracic paraplegia was an unavoidable consequence of his fall, not the result of wearing a Leatt- Brace®, and that the neck brace likely saved his life (or saved him from quadriplegia) by preventing cervical spine injury. The Company had maintained from the onset that this and a small handful of other lawsuits are without merit and that it will vigorously defend itself in each case. In this case, the plaintiffs subsequently appealed the court's decision and the parties reached an amicable settlement. Although we carry product liability insurance, a successful claim brought against us could significantly harm our business and financial condition and have an adverse impact on our ability to renew our product liability insurance or secure new coverage.

- Protection of Intellectual Property** We believe that the continued success of our business is dependent on our intellectual property portfolio consisting of globally registered trademarks, design patents and utility patents related to the Leatt-Brace®. We believe that a loss of these rights would harm or cause a material disruption to our business and, our corporate strategy is to aggressively take legal action against any violators of our intellectual property rights, regardless of where they may be. From time to time, we have had to enforce our intellectual property rights through litigation and we may be required to do so in the future. Such litigation may result in substantial costs and could divert resources and management attention from the operations of our business.

## Results of Operations

The following summary of our results of operations should be read in conjunction with our financial statements and the notes thereto for the three- and six-month periods ended June 30, 2016 and 2015 included herein. The following tables set forth key components of our results of operations for the periods indicated, both in dollars and as a percentage of sales revenue and key components of our revenue for the periods indicated in dollars and percentages.

### Three Months Ended June 30, 2016 compared to the Three Months Ended June 30, 2015

The following table summarizes the results of our operations during the three-month periods ended June 30, 2016 and 2015 and provides information regarding the dollar and percentage increase or (decrease) in such periods:

Item	Three Months Ended June 30,		\$ Increase	Percentage
	2016	2015	(Decrease)	Increase (Decrease)
REVENUES	\$ 3,693,915	\$ 5,193,056	\$ (1,499,141)	-29%
COST OF REVENUES	1,710,012	2,361,827	\$ (651,815)	-28%
GROSS PROFIT	1,983,903	2,831,229	\$ (847,326)	-30%
PRODUCT ROYALTY INCOME	39,649	20,668	\$ 18,981	92%
OPERATING EXPENSES				
Salaries and Wages	523,912	542,467	\$ (18,555)	-3%
Commissions and Consulting	133,921	151,468	\$ (17,547)	-12%
Professional Fees	70,659	246,392	\$ (175,733)	-71%
Advertising and Marketing	352,801	363,313	\$ (10,512)	-3%
Office Rent and Expenses	62,962	62,543	\$ 419	1%
Research and Development Costs	338,244	293,666	\$ 44,578	15%
Bad Debt Expense (Recovery)	(25,384)	19,461	\$ (44,845)	-230%
General and Administrative	514,852	489,116	\$ 25,736	5%
Depreciation	106,481	91,473	\$ 15,008	16%
Total Operating Expenses	2,078,448	2,259,899	\$ (181,451)	-8%
INCOME (LOSS) FROM OPERATIONS	(54,896)	591,998	\$ (646,894)	-109%
Other Income	70,750	7,539	\$ 63,211	838%
INCOME (LOSS) BEFORE INCOME				
TAXES	15,854	599,537	\$ (583,683)	-97%
Income Taxes	27,310	175,600	\$ (148,290)	-84%
NET INCOME (LOSS)	\$ (11,456)	\$ 423,937	\$ (435,393)	-103%

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**Revenues** We earn revenues from the sale of our protective gear, comprising of neck braces, body armor, helmets and other products, parts and accessories both in the United States and abroad. Revenues for the three months ended June 30, 2016 were \$3.7 million, a 29% decrease, compared to revenues of \$5.2 million for the quarter ended June 30, 2015. Revenues from sales to international customers were \$1.83 million and \$3.4 million, or 50% and 66% of revenues, respectively, for the three months ended June 30, 2016 and 2015. This decrease in revenues is primarily attributable to a \$1.16 million decrease in neck brace sales and a \$0.65 million decrease in body armor sales, that was partially offset by a \$0.37 million increase in helmet sales.

The following table sets forth our revenues by product line for the three months ended June 30, 2016 and 2015:

	Three Months Ended June 30,			
	2016	% of Revenues	2015	% of Revenues
Neck braces	\$ 1,300,052	35%	\$ 2,465,036	48%
Body armor	1,790,425	49%	2,443,161	47%
Helmets	374,659	10%	-	0%
Other products, parts and accessories	228,779	6%	284,859	5%
	\$ 3,693,915	100%	\$ 5,193,056	100%

Sales of our flagship neck brace accounted for \$1.3 million and \$2.47 million, or 35% and 48% of our revenues for the quarters ended June 30, 2016 and 2015, respectively. A 65% decrease in Neck brace sales volumes to our customers outside of the United States was the primary reason for the 47% decrease in neck brace revenues during the second quarter of 2016. This decrease is attributable to a 100% decrease in the volume of neck braces sold to our OEM customers outside of the United States during the second quarter of 2016, as well as the continued strengthening of the US dollar against the local currencies of our customers in Australasia and Europe when compared to the comparative period.

Our body armor products are comprised of chest protectors, full upper body protectors, upper body protection vests, back protectors, knee braces and knee and elbow guards. Body armor sales accounted for \$1.79 million and \$2.44 million, or 49% and 47% of our revenues for the quarters ended June 30, 2016 and 2015, respectively. The 27% decrease in body armor revenues was primarily the result of a 72% decrease in the volume of C-Frame knee braces shipped to our customers globally, when compared to the 2016 period. Initial stocking shipments of our C-Frame knee brace to our international customers were made during the third quarter of 2014 with further stocking shipments made in the first and second quarters of 2015. The strengthening of the US dollar discussed above has resulted in decreased sales and consequently increased inventory levels of C-Frame knee braces at the distributor level.

Our Helmets accounted for \$0.37 million, or 10% of our revenues for the three months ended June 30, 2016. The 100% increase in Helmet revenues is due to the continuation of the initial shipment of our GPX 5.5 Composite and GPX 6.5 Carbon helmets that first shipped to our customers in the United States and abroad during the fourth quarter of 2015. Additionally, we shipped DBX 6.0 Carbon helmets and DBX 5.0 Composite helmets to our international customers and in the United States during the second quarter of 2016.

Our other products, parts and accessories are comprised of aftermarket support items required primarily to replace worn or damaged parts through our global distribution network, as well as clothing, outerwear and accessories that include hats, jackets, bags, hydration kits and cooling garments. Other products, parts and accessories sales accounted for \$0.23 million and \$0.28 million, or 6% and 5% of our revenues for the quarters ended June 30, 2016 and 2015, respectively. The decrease in revenues from the sale of other products, parts and accessories is primarily due to a decrease in the volume of spare part units sold abroad during the period.

**Cost of Revenues and Gross Profit** Cost of revenues for the quarters ended June 30, 2016 and 2015 were \$1.7 million and \$2.4 million, respectively. Gross Profit for the quarters ended June 30, 2016 and 2015 were \$1.98 million and \$2.83 million, respectively, or 54% and 55% of revenues respectively. Our neck brace products continue to generate a higher gross margin than our other product categories. Neck brace revenues accounted for 35% and 48% of our

revenues for the quarters ended June 30, 2016 and 2015 respectively.

*Product Royalty Income* Product royalty income is earned on sales to distributors that have royalty agreements in place, as well as on sales of licensed products by third parties that have licensing agreements in place. Product royalty income for the quarters ended June 30, 2016 and 2015 were \$39,649 and \$20,668, respectively. The 92% increase in product royalty income is due to an increase in the sale of licensed products by licensees in the 2016 period.

*Salaries and Wages* Salaries and wages for the quarters ended June 30, 2016 and 2015 were \$523,912 and \$ 542,467, respectively. This 3% decrease in salaries and wages during the 2016 period was primarily due to the restructuring of our operational functions in the United States.

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*Commissions and Consulting Expense* During the quarters ended June 30, 2016 and 2015, commissions and consulting expenses were \$133,921 and \$151,468, respectively. This 12% decrease in commissions and consulting expenses is primarily the result of lower commissions paid to sales representatives in both the United States and abroad as a result of the decreased sales revenues discussed above.

*Professional Fees* Professional fees consist of costs incurred for audit, tax and regulatory filings, as well as patent protection and product liability litigation expenses incurred as the Company continues to expand. Professional fees for the quarters ended June 30, 2016 and 2015 were \$70,659 and \$246,392, respectively. This 71% decrease in professional fees is primarily due to decreased spending on product liability litigation during the 2016 period.

*Advertising and Marketing* The Company places paid advertising in various motorsport magazines and online media, and sponsors a number of events, teams and individuals to increase product and brand visibility. Advertising and marketing expenses for the quarters ended June 30, 2016 and 2015 were \$352,801 and \$363,313, respectively. The 3% decrease in advertising and marketing expenditures during the 2016 period is primarily due to a continued focus on improving the efficacy of its global athlete sponsorship programs.

*Office Rent and Expenses* Office rent and expenses for the quarters ended June 30, 2016 and 2015 remained flat at \$62,962 and \$62,543, respectively.

*Research and Development Costs* These costs consist of the salaries of personnel who are directly involved in the research and development of innovative products, as well as the direct costs associated with developing these products. Research and development costs for the quarters ended June 30, 2016 and 2015, increased to \$338,244, from \$293,666, during the same 2015 quarter. The 15% increase in research and development costs is a result of costs incurred to widen the Company's product range, as well as the employment of additional design and development resources.

*Bad Debt Expense (Recovery)* Bad Debt Expense (Recovery) for the quarters ended June 30, 2016 and 2015 were (\$25,384) and \$19,461, respectively. This 230% decrease in Bad Debt Expense (Recovery) is primarily the result of the write off of a portion of unrecoverable debt owed to Two Eleven during the 2015 comparative period.

*General and Administrative Expenses* General and administrative expenses consist of insurance, travel, merchant fees, telephone, office and computer supplies. General and administrative expenses for the quarters ended June 30, 2016 and 2015 were \$514,852 and \$489,116, respectively. The 5% increase in general and administrative expenses is primarily as a result of increased travel costs incurred by the Company's sales and marketing team in the United States in connection with travel activities designed to improve the Company's dealer merchandising and event presence.

*Depreciation Expense* Depreciation Expense for the quarters ended June 30, 2016 and 2015 were \$106,481 and \$91,473, respectively. This 16% increase in depreciation is primarily as a result of the addition of molds and tooling required for the production of the Company's widening product range.

*Total Operating Expenses* Total operating expenses decreased by \$181,451, to \$2.08 million in the three months ended June 30, 2016, or 8%, compared to \$2.26 million in the 2015 period. This decrease is primarily due to decreased professional fees and salaries and wages that were partially offset by an increase in research and development costs and increased general and administrative costs.

*Net income (loss)* The net loss after income taxes for the quarter ended June 30, 2016 was (\$11,456) as opposed to a net income after income taxes of \$423,937 for the quarter ended June 30, 2015. This decrease in net income (loss) is primarily due to the decrease in revenues discussed above.

***Six Months Ended June 30, 2016 Compared to the Six Months Ended June 30, 2015***



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The following table summarizes the results of our operations during the six-month periods ended June 30, 2016 and 2015 and provides information regarding the dollar and percentage increase or (decrease) in such periods:

- 15 -

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Item	Six Months Ended June 30,		\$ Increase (Decrease)	Percentage Increase (Decrease)
	2016	2015		
REVENUES	\$ 8,521,407	\$ 9,214,511	\$ (693,104)	-8%
COST OF REVENUES	4,023,669	4,206,022	\$ (182,353)	-4%
GROSS PROFIT	4,497,738	5,008,489	\$ (510,751)	-10%
PRODUCT ROYALTY INCOME	53,531	72,201	\$ (18,670)	-26%
OPERATING EXPENSES				
Salaries and Wages	1,205,214	1,148,645	\$ 56,569	5%
Commissions and Consulting	299,992	337,376	\$ (37,384)	-11%
Professional Fees	252,318	461,165	\$ (208,847)	-45%
Advertising and Marketing	714,394	624,755	\$ 89,639	14%
Office Rent and Expenses	127,152	123,051	\$ 4,101	3%
Research and Development Costs	681,059	586,383	\$ 94,676	16%
Bad Debt Expense (Recovery)	(22,557)	19,461	\$ (42,018)	-216%
General and Administrative	961,798	914,332	\$ 47,466	5%
Depreciation	210,998	184,276	\$ 26,722	15%
Total Operating Expenses	4,430,368	4,399,444	\$ 30,924	1%
INCOME FROM OPERATIONS	120,901	681,246	\$ (560,345)	-82%
Other Income	68,809	7,981	\$ 60,828	762%
INCOME BEFORE INCOME TAXES	189,710	689,227	\$ (499,517)	-72%
Income Taxes	88,186	211,185	\$ (122,999)	-58%
NET INCOME	\$ 101,524	\$ 478,042	\$ (376,518)	-79%

*Revenues* Revenues for the six-month periods ended June 30, 2016 were \$8.5 million, an 8% decrease, compared to revenues of \$9.2 million for the quarter ended June 30, 2015. Revenues associated with international customers were \$4.8 million and \$5.9 million, or 56% and 64% of revenues, respectively, for the six months ended June 30, 2016 and 2015. This decrease in revenues is attributable to a \$1.36 million decrease in neck brace sales and a \$0.48 million decrease in body armor sales, which was partially offset by a \$1.18 million increase in helmet sales.

The following table sets forth our revenues by product line for the six months ended June 30, 2016 and 2015:

	Six Months Ended June 30,			
	2016	% of Revenues	2015	% of Revenues
Neck braces	\$ 2,893,782	34%	\$ 4,254,644	46%
Body armor	3,980,901	47%	4,458,073	48%
Helmets	1,183,214	14%	-	0%
Other products, parts and accessories	463,510	5%	501,794	6%
	\$ 8,521,407	100%	\$ 9,214,511	100%

Sales of our flagship neck brace accounted for \$2.89 million and \$4.25 million, or 34% and 46% of our revenues for the six-month periods ended June 30, 2016 and 2015, respectively. A 49% decrease in Neck brace sales volumes to our customers outside of the United States was the primary reason for the 32% decrease in neck brace revenues during the six months ended June 30, 2016. This decrease is attributable to a 100% decrease in the volumes of neck braces sold to our OEM customers outside of the United States during the six months ended June 30, 2016, as well as the continued strengthening of the US dollar against the local currencies of our customers in Australasia and Europe when compared to the comparative prior period.

Body armor sales accounted for \$3.98 million and \$4.46 million, or 47% and 48% of our revenues for the six-month periods ended June 30, 2016 and 2015, respectively. The 11% decrease in body armor revenues was primarily the result of a 67% decrease in the volume of C-Frame knee braces shipped to our customers globally. Initial stocking shipments of our C-Frame knee brace to our international customers were made during the third quarter of 2014, with

further stocking shipments made in the first and second quarters of 2015. The strengthening of the US dollar discussed above has resulted in decreased sales and consequently increased inventory levels of C-Frame knee braces at the distributor level. Management continues to monitor currency fluctuations globally and evaluate marketing and sales strategies accordingly.

Our Helmets accounted for \$1.18 million, or 14% of our revenues for the six months ended June 30, 2016. The 100% increase in Helmet revenues is due to the continuation of the initial shipment of our GPX 5.5 Composite and GPX 6.5 Carbon helmets that first shipped to our customers in the United States and abroad during the fourth quarter of 2015. Additionally, we shipped the DBX 6.0 Carbon helmets and DBX 5.0 Composite helmets to our international customers and in the United States during the first half of 2016.

Other products, parts and accessories sales accounted for \$0.46 million and \$0.50 million, or 5% and 6% of our revenues for the six-month periods ended June 30, 2016 and 2015, respectively. The decrease in revenues from the sale of other products, parts and accessories is primarily due to a decrease in the volume of spare parts units sold abroad during the period.

*Cost of Revenues and Gross Profit* Cost of revenues for the six-months ended June 30, 2016 and 2015 were \$4.0 million and \$4.2 million, respectively. Gross Profit for the six-month periods ended June 30, 2016 and 2015 were \$4.5 million and \$5.0 million, respectively, or 53% and 54% of revenues, respectively. However, our neck brace products continue to generate a higher gross margin than our other product categories. Neck brace revenues accounted for 34% and 46% of our revenues for the six months ended June 30, 2016 and 2015, respectively.

*Product Royalty Income* Product royalty income is earned on sales to distributors that have royalty agreements in place, as well as on sales of licensed products by third parties that have licensing agreements in place. Product royalty income for the six-month periods ended June 30, 2016 and 2015 were \$53,531 and \$72,201, respectively. The 26% decrease in product royalty income is due to a decrease in the sale of licensed products by licensees in the 2016 period.

*Salaries and Wages* Salaries and wages for the six-month periods ended June 30, 2016 and 2015 were \$1,205,214 and \$1,148,645, respectively. This 5% increase in salaries and wages during the 2016 period was primarily due to the vesting of share options issued to key personnel during the six-month period ended June 30, 2016.

*Commissions and Consulting Expense* During the six-month periods ended June 30, 2016 and 2015, commissions and consulting expenses were \$299,992 and \$337,376, respectively. This 11% decrease in commissions and consulting expenses is primarily the result of lower commissions paid to sales representatives in both the United States and abroad as a result of the decreased sales revenues discussed above.

*Professional Fees* Professional fees consist of costs incurred for audit, tax and regulatory filings, as well as patent protection and product liability litigation expenses incurred as the Company continues to expand. Professional fees for the six-month periods ended June 30, 2016 and 2015 were \$252,318 and \$461,165, respectively. This 45% decrease in professional fees is primarily due to decreased spending on product liability litigation during the 2016 period.

*Advertising and Marketing* The Company places paid advertising in various motorsport magazines and online media, and sponsors a number of events, teams and individuals to increase product and brand visibility. Advertising and marketing expenses for the six-months ended June 30, 2016 and 2015 were \$714,394 and \$624,755, respectively. The 14% increase in advertising and marketing expenditures during the 2016 period is primarily due to the Company's continued implementation of sponsorship, advertising and marketing campaigns designed to promote the Company's widening product categories and brand.

*Office Rent and Expenses* Office rent and expenses for the six-month periods ended June 30, 2016 and 2015 remained flat at \$127,152 and \$123,051, respectively.

*Research and Development Costs* These costs consist of the salaries of personnel who are directly involved in the research and development of innovative products, as well as the direct costs associated with developing these products. Research and development costs for the six-month periods ended June 30, 2016 and 2015, increased to \$681,059, from \$586,383, during the same 2015 period. The 16% increase in research and development costs is a result of costs incurred to widen the Company's product range, as well as the employment of additional design and development resources.

*Bad Debt Expense (Recovery)* Bad Debt Expense (Recovery) for the six-month periods ended June 30, 2016 and 2015 were (\$22,557) and \$19,461, respectively. This 216% decrease in Bad Debt Expense (Recovery) is primarily the result of the write off of a portion of unrecoverable debt owed to Two Eleven during the 2015 comparative period.

*General and Administrative Expenses* General and administrative expenses consist of insurance, travel, merchant fees, telephone, office and computer supplies. General and administrative expenses for the six-month periods ended June 30, 2016 and 2015 were \$961,798 and \$ 914,332, respectively. The 5% increase in general and administrative expenses is primarily as a result of increased travel expenditure required in the development of the Company's growing product range as well as in order to continue the activation of the Company's store merchandising and event presence in the United States.

*Depreciation Expense* Depreciation Expense for the six-month periods ended June 30, 2016 and 2015 were \$210,998 and \$ 184,276, respectively. This 15% increase in depreciation is primarily as a result of the addition of molds and tooling required for the production of the Company's widening product range.

*Total Operating Expenses* Total operating expenses increased by \$30,924, to \$4.43 million in the six month periods ended June 30, 2016, or 1%, compared to \$4.40 million in the 2015 period. This increase is primarily due to increased research and development and advertising and marketing costs and were partially offset by decreased professional fees discussed above.

*Net income* The net income after income taxes for the six-month periods ended June 30, 2016 was \$101,524 as opposed to a net income after income taxes of \$478,042 for the six-month periods ended June 30, 2015. This decrease in net income is primarily due to decreased revenues discussed above.

### **Liquidity and Capital Resources**

At June 30, 2016, we had cash and cash equivalents of \$1 million and \$0.06 million of short-term investments. The following table sets forth a summary of our cash flows for the periods indicated:

- 17 -

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	<b>June 30,</b>	
	<b>2016</b>	<b>2015</b>
Net cash provided by operating activities	\$ 331,894	\$ 949,764
Net cash used in investing activities	\$ (52,641)	\$ (53,680)
Net cash used in financing activities	\$ (348,014)	\$ (334,557)
Effect of exchange rate changes on cash and cash equivalents	\$ 14,770	\$ (67,271)
Net increase (decrease) in cash and cash equivalents	\$ (53,991)	\$ 494,256
Cash and cash equivalents at the beginning of period	\$ 1,054,750	\$ 724,707
Cash and cash equivalents at the end of period	\$ 1,000,759	\$ 1,218,963

Cash decreased by \$53,991, or 5%, for the six months ended June 30, 2016. The primary sources of cash for the six months ended June 30, 2016 were a net income of \$101,524, decreased accounts receivables of \$846,161, and decreased prepaid expenses and other current assets of \$363,114. The primary uses of cash for the six months ended June 30, 2016 were decreased accounts payable and accrued expenses of \$1,055,229 and the repayment of a short-term loan amounting to \$387,014. As of June 30, 2016, we did not have any credit facilities or significant amounts owed to third party lenders.

The Company is currently meeting its working capital needs through cash on hand as well as internally generated cash from operations. Management believes that its current cash and cash equivalent balances, along with the net cash generated by operations are sufficient to meet its anticipated operating cash requirements for at least the next twelve months. There are currently no plans for any major capital expenditures in the next twelve months. Our long-term financing requirements depend on our growth strategy, which relates primarily to our desire to increase revenue both in the U.S. and abroad.

#### **Obligations under Material Contracts**

Pursuant to our Licensing Agreement with Xceed Holdings, a company owned and controlled by Dr. Christopher Leatt, our founder and chairman, we pay Xceed Holdings, 4% of all neck brace sales revenue billed and received by the Company on a quarterly basis, based on sales of the previous quarter. In addition, pursuant to a separate license agreement between the Company and Mr. J. P. De Villiers, our former director, the Company is obligated to pay a royalty fee of 1% of all our billed and received neck brace sales revenue, in quarterly installments, based on sales of the previous quarter, to a trust that is beneficially owned and controlled by Mr. De Villiers.

Pursuant to a Premium Finance Agreement, dated October 19, 2015, between the Company and AFCO Acceptance Corporation AFCO, the Company is obligated to pay AFCO an aggregate sum of \$ 852,081 in eleven payments of \$71,952, at an annual interest rate of 2.897%, commencing on November 1, 2015 and ending on September 1, 2016. Any late payment during the term of the agreement will be assessed a late penalty of 5% of the payment amount due, and in the event of default AFCO has the right to accelerate the payment due under the agreement. As of June 30, 2016, the Company had not defaulted on its payment obligations under this agreement.

Pursuant to a Premium Finance Agreement, dated May 9, 2016, between the Company and AFCO, the Company is obligated to pay AFCO an aggregate sum of \$59,120 in eleven payments of \$5,375 at a 3.397% annual interest rate, commencing on June 1, 2016 and ending on April 1, 2017. Any late payment during the term of the agreement will be assessed a late penalty of 5% of the payment amount due, and in the event of default AFCO has the right to accelerate the payment due under the agreement. As of June 30, 2016, the Company had not defaulted on its payment obligations under this agreement.

On July 8, 2015, the Company entered into a consulting agreement with Innovate Services Limited, or Innovate, a Seychelles limited company in which, Dr. Leatt is an indirect beneficiary. Pursuant to the terms of the Consulting Agreement, Innovate has agreed to serve as the Company's exclusive research, development and marketing consultant, in exchange for a monthly fee of \$35,639; provided that Dr. Leatt personally performs the services to be performed by Innovate under the Agreement, pursuant to a separate employment agreement between Innovate and Dr. Leatt. The

parties further agreed that all intellectual property generated in connection with the services provided under the Consulting Agreement will be the sole property of the Company. The Consulting Agreement was effective as of May 15, 2015, and will continue unless terminated by either party in accordance with its terms. Either party has the right to terminate the Consulting Agreement upon 6 months' prior written notice, except that the Consulting Agreement may be terminated immediately without notice if the services to be performed under the Consulting Agreement cease to be performed by Dr. Leatt, or for any other material breach of the Agreement. The parties have agreed to settle any dispute under the Consulting Agreement through arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association (AAA), and that the resulting arbitration award will be final and binding on both parties and will not be subject to any appeal. The foregoing description does not purport to be a complete statement of the parties' rights and obligations under the Consulting Agreement and the transactions contemplated thereby or a complete explanation of the materials thereof.

## Critical Accounting Policies

Our discussion and analysis of financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements 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 financial statements and the reported revenues and expenses during the reporting period. We have identified the following as the items that require the most significant judgment and often involve complex estimation: revenue recognition, estimating allowances for doubtful accounts receivable, inventory valuation, impairment of long-lived assets and accounting for income taxes.

**Revenue and Cost Recognition** - All manufacturing of Leatt-Brace products is performed by third party subcontractors in China. The Company's products are sold worldwide to a global network of distributors and dealers, and directly to consumers when there are no dealers or distributors in their geographic area (collectively the "customers"). Revenues from product sales are recognized when earned, net of applicable provisions for discounts and returns and allowances in the event of product defect. Revenue is considered to be realized or realizable and earned when all of the following criteria are met: title and risk of loss have passed to the customer, persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed and determinable and collectability is reasonably assured. Our distributor payment terms range from pre-payment in full to 60 days after shipment and subsequent sales of our products by distributors have no effect on the amount and timing of payments due to us. Furthermore, products purchased by distributors may not be returned to us in the event that any such distributor relationship is terminated.

Since the Company (through its wholly-owned subsidiary) serves as the distributor of Leatt products in the United States, the Company records its revenue and related cost of revenue for its product sales in the United States upon shipment of the merchandise to the dealer or to the ultimate consumer when there is no dealer in the geographic area and the sales order was received directly from, and paid by, the ultimate consumer. Since the Company (through its South African branch) serves as the distributor of Leatt products in South Africa, the Company records its revenue and related cost of revenue for its product sales in South Africa upon shipment of the merchandise from the branch to the dealer. International sales (other than in South Africa) are generally drop-shipped directly from the third party manufacturer to the international distributors.

Revenue and related cost of revenue is recognized at the time of shipment from the manufacturer's port when the shipping terms are Free On Board ("FOB") shipping point. Cost and Freight ("CFR") or Cost and Insurance to named place ("CIP") as legal title and risk of loss to the product pass to the distributor. Sales to all customers (distributors, dealers and consumers) are generally final; however, in limited instances, product may be returned due to product quality issues. Historically, returns due to product quality issues have not been material and there have been no distributor terminations that resulted in product returns. Cost of revenues also includes royalty fees associated with sales of Leatt-Brace products. Product royalty income is recorded as the underlying product sales occur, in accordance with the related licensing arrangements.

**Allowance for Doubtful Accounts Receivable** - Accounts receivable consist of amounts due to the Company from normal business activities. Credit is granted to substantially all distributors on an unsecured basis. We continuously monitor collections and payments from customers and maintain an allowance for doubtful accounts receivable based upon historical experience and any specific customer collection issues that have been identified. In determining the amount of the allowance, we are required to make certain estimates and assumptions. Accounts receivable balances that are still outstanding after we have used reasonable collection efforts are written off as uncollectible. While such credit losses have historically been minimal, within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. A significant change in the liquidity or financial position of any of our significant customers could have a material adverse effect on the collectability of our accounts receivable and our future operating results.



**Inventory Valuation** Inventory is stated at the lower of cost or market. Cost is determined using the first-in first-out (FIFO) method. Inventory consists primarily of finished goods. Shipping and handling costs are included in the cost of inventory. In assessing the inventory value, we make estimates and judgments regarding reserves required for product obsolescence, aging of inventory and other issues potentially affecting the saleable condition of products. In performing such evaluations, we utilize historical experience as well as current market information. The reserve for obsolescence as of the six-month periods ended June 30, 2016 and 2015 was \$173,695 and \$322,355, respectively.

**Impairment of Long-Lived Assets** Our long-lived assets include property and equipment. We evaluate our long-lived assets for recoverability whenever events or changes in circumstances indicate that an asset may be impaired. In evaluating an asset for recoverability, we estimate the future cash flow expected to result from the use of the asset and eventual disposition. If the expected future undiscounted cash flow is less than the carrying amount of the asset, an impairment loss, equal to the excess of the carrying amount over the fair value of the asset, is recognized. We have determined there was no impairment charge during the six-month periods ended June 30, 2016 and 2015.

**Income Taxes** - As part of the process of preparing our consolidated financial statements, we are required to estimate our income tax provision (benefit) in each of the jurisdictions in which we operate. This process involves estimating our current income tax provision (benefit) together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets. We regularly evaluate our ability to recover the reported amount of our deferred income taxes considering several factors, including our estimate of the likelihood of the Company generating sufficient taxable income in future years during the period over which the temporary differences reverse.

### **Recent Accounting Pronouncements**

See Note 8, Summary of Significant Accounting Policies in the Notes to Consolidated Financial Statements for a full description of recent accounting pronouncements, including the respective dates of adoption, or expected adoption and effects of our consolidated financial position, results of operations and cash flows.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to its stockholders.

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

Not Applicable.

### **ITEM 4. CONTROLS AND PROCEDURES.**

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

As of June 30, 2016, the Company's management, under the direction of its Chief Executive Officer and the Chief Financial Officer, Mr. Sean Macdonald, carried out an evaluation of the effectiveness of the design and operation of the disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in our SEC reports is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms, and is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer determined that the Company's disclosure controls and procedures were deemed to be effective.

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

There were no changes in our internal controls over financial reporting during the period ended June 30, 2016, that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **PART II** **OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS.**

From time to time, we may become involved in various lawsuits and legal proceedings in the ordinary course of our business. Other than as set forth below, we are currently not aware of any legal proceedings the ultimate outcome of which, in our judgment based on information currently available, would have a material adverse effect on our business, financial condition or operating results.

On February 25, 2015, a lawsuit was filed against the Company on behalf of a motorcycle rider in the Northern District Court of Indiana, Lafayette Division for strict liability, breach of warranty, negligence, punitive damages and deceptive and misleading advertising and marketing. The litigation is at discovery stage and the trial is currently scheduled to commence October 30, 2017. The Company believes that the lawsuit is without merit and intends to vigorously defend itself.

### **ITEM 1A. RISK FACTORS.**

There are no material changes from the risk factors previously disclosed in Item 1A Risk Factors of our annual report on Form 10-K for the period ended December 31, 2015.

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

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES.**

None.

**ITEM 4. MINE SAFETY DISCLOSURES.**

None.

**ITEM 5. OTHER INFORMATION.**

We have no information to disclose that was required to be in a report on Form 8-K during the period covered by this report, but was not reported. There have been no material changes to the procedures by which security holders may recommend nominees to our board of directors.

**ITEM 6. EXHIBITS.**

The following exhibits are filed as part of this report or incorporated by reference:

**Exhibit Description**

<b>No.</b>	<b>Description</b>
<u>31.1</u>	<u>Certifications of Principal Executive Officer filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>
<u>31.2</u>	<u>Certifications of Principal Financial Officer filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>
<u>32.1</u>	<u>Certifications of Principal Executive Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u>
<u>32.2</u>	<u>Certifications of Principal Financial Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u>
101*	Interactive data files pursuant to Rule 405 of Regulation S-T

\* Filed with this Form 10-Q for Leatt Corporation. Pursuant to Rule 406T of Regulation S-T, the interactive data files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, or for purposes of Section 18 of the Securities Act of 1934, as amended, and otherwise are not subject to liability under those sections.

**SIGNATURES**

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: August 12, 2016

**LEATT CORPORATION**

By: /s/ Sean Macdonald

Sean Macdonald

Chief Executive Officer and Chief Financial Officer

*(Principal Executive, Financial and Accounting Officer)*

- 22 -

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EXHIBIT INDEX

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