Lumber Liquidators, Inc.
Form S-1/A
June 15, 2007
Table of Contents

As filed with the Securities and Exchange Commission on June 15, 2007

Registration No. 333-142309

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

AMENDMENT NO. 2

TO

FORM S-1

REGISTRATION STATEMENT

UNDER THE SECURITIES ACT OF 1933

LUMBER LIQUIDATORS, INC.

(Exact name of Registrant as specified in its charter)

Massachusetts	**5211**	**043229199**
(State or other jurisdiction of incorporation or organization)	**(Primary Standard Industrial Classification Code Number)**	**(I.R.S. Employer Identification No.)**

3000 John Deere Road

Toano, Virginia 23168

(757) 259-4280

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

E. Livingston B. Haskell

General Corporate Counsel

Lumber Liquidators, Inc.

3000 John Deere Road

Toano, Virginia 23168

(757) 259-4280

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Jeffrey D. Karpf, Esq.

Cleary Gottlieb Steen & Hamilton LLP

One Liberty Plaza

New York, NY 10006

(212) 225-2000

Robert E. Buckholz, Jr., Esq.

Sullivan & Cromwell LLP

125 Broad Street

New York, NY 10004-2498

(212) 558-4000

Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this Registration Statement.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. ¨

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

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

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

CALCULATION OF REGISTRATION FEE

Title of each class of securities to be registered	**Proposed maximum aggregate offering price(1)(2)**	**Amount of registration fee**
Common Stock, no par value	$150,000,000	$4,605(3)

(1) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(o) under the Securities Act.

(2) Includes (i) shares of common stock to be offered by the registrant and the selling stockholders in this offering and (ii) shares of common stock that may be purchased by the underwriters from the selling stockholders upon the exercise of the underwriters option to purchase additional shares.

(3) Previously paid.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this preliminary prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell nor does it seek an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

Subject to Completion. Dated June 15, 2007

Shares

Lumber Liquidators, Inc.

Common Stock

This is an initial public offering of shares of common stock of Lumber Liquidators, Inc.

Lumber Liquidators, Inc. is offering of the shares to be sold in the offering. The selling stockholders identified in this prospectus, including the chairman of our board of directors, are offering an additional shares. Lumber Liquidators, Inc. will not receive any of the proceeds from the sale of the shares being sold by the selling stockholders.

Prior to this offering, there has been no public market for the common stock. We currently estimate that the initial public offering price per share will be between $ and $. We will apply to list the common stock on the New York Stock Exchange under the symbol LL.

See Risk Factors beginning on page 10 to read about factors you should consider before buying shares of the common stock.

Neither the Securities and Exchange Commission nor any state securities commission nor any other regulatory body has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per Share	Total
Initial public offering price	$	$
Underwriting discount	$	$
Proceeds, before expenses, to Lumber Liquidators, Inc.	$	$
Proceeds, before expenses, to the selling stockholders	$	$

To the extent that the underwriters sell more than shares of common stock, the underwriters have the option to purchase up to an additional shares of common stock from the selling stockholders at the initial public offering price less the underwriting discount.

The underwriters expect to deliver the shares of common stock against payment in New York, New York on , 2007.

Goldman, Sachs & Co. **Merrill Lynch & Co.**

Lehman Brothers

Banc of America Securities LLC

Piper Jaffray & Co.

Prospectus dated , 2007.

Table of Contents

Table of Contents

Table of Contents

TABLE OF CONTENTS

Table of Contents

PROSPECTUS SUMMARY

The following summary highlights information appearing elsewhere in this prospectus. This summary does not contain all of the information you should consider before investing in our common stock. You should read this entire prospectus carefully. In particular, you should read the sections entitled Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and the notes relating to those statements.

The Company

Lumber Liquidators is the largest specialty retailer of hardwood flooring in the United States, based on industry sources and our experience. We believe we have achieved a reputation for offering great value, superior service and a broad selection of high-quality hardwood flooring products. We offer an extensive selection of premium hardwood flooring products under multiple proprietary brands at everyday low prices designed to appeal to a diverse customer base. We believe that our vertically integrated business model enables us to offer a broad assortment of high-quality products to our customers at a lower cost than our competitors. As of May 31, 2007, we sold our products through 98 Lumber Liquidators stores in 40 states, a call center, our website and a catalog. We believe that our brands, value proposition and integrated multi-channel approach are important competitive advantages.

We offer hardwood flooring products from more than 25 domestic and exotic wood species in both prefinished and unfinished brands of various widths and lengths. Our products are differentiated in terms of quality and price based on the species, grade of the hardwood, quality of finishing, as well as the length of the warranty. We also offer a broad assortment of flooring enhancements and installation accessories including moldings, noise-reducing underlays and adhesives. Our product offering is substantially comprised of our proprietary brands, including our premium Bellawood brand as well as our Builder s Pride, Schôn, Morning Star Bamboo and Dream Home brands. We have experienced strong historical growth, including net sales growth from $171.8 million in 2004 to $332.1 million in 2006, operating income growth from $7.2 million in 2004 to $21.4 million in 2006 and net income growth from $8.0 million in 2004 to $12.9 million in 2006, representing compound annual growth rates of approximately 39%, 73% and 27%, respectively. In the first quarter of 2007, our net sales were $92.0 million, which represents a 21% increase over the first quarter of 2006. Our operating income for the first quarter of 2007 declined to $3.8 million from $5.9 million in the first quarter of 2006, and our net income declined to $2.2 million from $3.6 million for the same periods. Our overall growth has been driven in large part by the opening of 74 stores since January 1, 2003 and our strong comparable store sales performance in each of those periods. On an annual basis, comparable store sales increased 19.0% from 2004 to 2005, and 17.3% from 2005 to 2006. In the first quarter of 2007, comparable store sales increased 8.5% over the first quarter of 2006, which increased 24.1% over the first quarter of 2005.

Our company started in 1994 when Tom Sullivan, the chairman of our board of directors, began selling discounted building materials. In 1996, he identified an opportunity to sell hardwood flooring at liquidator prices. Tom observed that traditional home improvement and flooring retailers underserved customers in terms of price, selection, product quality and overall value. Tom began working directly with vendors and mills to provide customers with broad, high-quality assortments at everyday low prices including premium categories. Since our first retail store opened in 1996, we have developed a national store base. Approximately 80% of our sales are to existing homeowners engaged in remodeling projects, and the remainder are to small independent contractors engaged in remodeling and new home-building projects. In 2004, we moved to our Toano, Virginia distribution center and finishing facility, where we currently finish 75% of our premium Bellawood products. We maintain our in-house finishing capability to ensure product quality and to reduce third-party finishing costs.

We have made a significant investment in developing our national brands, including our portfolio of proprietary product offerings. We believe Lumber Liquidators is now recognized across the United States as a destination for high-quality hardwood flooring at everyday low prices, while our Bellawood brand is known as a premium flooring brand within the industry. Our stores typically consist of a warehouse and an attached showroom located in industrial or commercial areas that have lower rents than traditional retail locations, are accessible from major roadways and have significant visibility to passing traffic. Our average store is approximately 6,000 square feet, of which approximately 800 square feet is devoted to the showroom selling area. We have designed our stores using a visually appealing and distinctive showroom format to enhance the customer experience while demonstrating our low-cost approach to doing business. We employ knowledgeable sales staff who can educate our customers about the product. We believe that our stores reinforce our customers belief that they get a good deal when they buy from us.

From 1994 until 2004, Tom Sullivan was our sole shareholder and director. In December 2004, we issued approximately 7.9 million shares of convertible preferred stock to funds managed by TA Associates, Inc., a private equity investment firm, in return for $35.0 million. Immediately prior to the issuance of those shares, which are convertible into shares of common stock on a one-to-one basis, we implemented a 150,000 to 1 stock split to increase the number of common shares held by Tom from 100 to approximately 15.0 million. After completion of the initial public offering, Tom and TA Associates, each of whom is a selling stockholder, will control approximately % and % of our outstanding common stock, respectively (or % and %, respectively, if the underwriters overallotment option is exercised in full), which also reflects the transfer of an estimated million shares from Tom to Kevin Sullivan pursuant to an existing stock-based compensation agreement between them. During the periods in which Tom was the sole shareholder, we made cash distributions to him from time to time, including amounts to enable him to pay taxes on deemed income during the period when we were an S corporation (from inception until December 2004). We distributed $42.6 million in cash to Tom in 2004, including $30.0 million of the proceeds from the sale of the convertible preferred stock (which represented a significant dilution of his ownership interest), $5.0 million to enable him to pay taxes on deemed income and $7.6 million of additional cash. As a result of these transactions, we had a total stockholder s deficit of $30.2 million as of December 31, 2004, which has steadily improved to a stockholder s deficit of $2.8 million as of March 31, 2007. We have not made any other cash or equity distributions to our directors, executive officers or other employees in the past three years (other than paying salaries and making equity-based compensation grants in the ordinary course), and no directors, officers or employees other than Tom receive any proceeds from this offering.

Competitive Strengths

We believe the following competitive strengths contribute to our leading market position, differentiate us from our competition and will drive our future growth:

Attractive Store Economics. We operate a store model that produces strong returns on investment by combining low capital investment, a small store footprint, minimal staffing and a high average sale of more than $1,700 in 2006. Our average new store across our markets has historically become profitable within three months of beginning operations and returned its initial cash investment within seven months. Our store model targets a pre-tax return on invested capital in excess of 140% for stores open more than three years (including all advertising costs). For the twelve months ended March 31, 2007, we did not have an unprofitable store on a four-wall basis in our portfolio (excluding stores open for less than three months). When measuring profitability on a four-wall basis, we take into account the sales and costs of sales at each individual store, as well as the expenses of that store, which include wages and benefits, rent and local advertising. We do not consider national advertising and store support costs, including those related to corporate overhead and our distribution facility, when calculating profitability on a four-wall basis.

Appealing Value Proposition. Our value proposition to the customer is a key driver of our business. Important components include:

Price. A fundamental part of our founding philosophy is to provide quality hardwood flooring brands at everyday low prices. We are able to maintain these prices across our product range because we purchase flooring directly from mills and brokers. In addition, we operate a low-cost store model with a no frills showroom, limited in-store inventory and locations in industrial or commercial areas that carry lower rent expense than many retail stores.

Selection. We have developed a broad product assortment of domestic and exotic hardwoods sold under proprietary brands that help us to differentiate our products from those of our competitors. We offer products across a range of price points and quality levels that allow us both to target discrete market segments and to appeal to diverse groups of customers.

Quality. We believe that we have achieved a reputation for quality, and that our proprietary brands are recognized for excellence by our customers. We work directly with our supplier mills and brokers to produce flooring that will meet our high quality standards and we also currently finish 75% of our premium Bellawood products at our state-of-the-art Toano facility. We maintain an in-house inspection and quality control function and enforce strict certification requirements for Bellawood supplier mills. As a result, we offer a 50-year residential warranty on our premier Bellawood brands, which we believe is the industry s longest.

Availability. Since our founding, we have made it a priority to build long-term relationships with our key supplier mills and brokers. As we have grown, we believe our relationships with our suppliers have strengthened, which we believe helps us ensure our continued access to a broad selection of domestic and exotic hardwood products at attractive prices. We believe that these direct supplier relationships are relatively unique in our industry, and offer us a significant competitive advantage. In addition, we believe our supply chain and centralized inventory at our Toano distribution facility allow us to meet the delivery needs of our customers better than our competitors.

Established National Brands. We believe both Lumber Liquidators and Bellawood are well-known national brands. We have positioned Lumber Liquidators to represent an attractive value proposition to the customer, and believe we offer superior service and hardwood flooring expertise. Based on our market research, we believe that Bellawood, which accounted for approximately one-third of our 2006 net sales, is among the most-recognized brands in our industry. We are committed to supporting our brands and products through diverse national marketing campaigns that reach a wide variety of potential customers. We believe that we benefit from our long-term endorsement relationships with respected and well-known home improvement celebrities such as Bob Vila and Ty Pennington.

Integrated Multi-Channel Sales Model. We have an integrated multi-channel sales model that enables our national store network, call center, website and catalog to work together in a coordinated manner. Our sales strategy emphasizes customer service by providing superior convenience and education tools for our customers to learn about our products and the installation process. We strive to use our various sales channels to make our customers transactions easy and efficient.

Table of Contents

Experienced Management Team with a Proven Track Record. Our senior management team has extensive experience with publicly traded, high-growth retail companies. We believe our company benefits in particular from the leadership of Tom Sullivan, our founder and the chairman of our board of directors, who is a veteran of the specialty hardwood flooring retail business. Jeff Griffiths, our president and chief executive officer, has more than 30 years of experience in the retail industry and our chief financial officer, Dan Terrell, has more than 15 years of experience working with reporting companies in the retail industry. Over the past 18 months, we have assembled a management team that has extensive experience in the specialty retail and hardline retail industries. Upon completion of this offering, our executive officers and directors will own % of our company.

Growth Strategy

We intend to continue to increase revenues and profitability by strengthening our position as a leading provider of hardwood flooring within our growing market. Specific elements of our strategy for continued growth include the following:

Expand Our Store Base. The hardwood flooring market is highly fragmented, and we believe there is a significant opportunity to expand our store base. Because of the low capital investment to open new stores and the attractive returns on investment that our stores generate, we intend to continue to expand our store base. We plan to open at least 25 new stores in 2007 and between 30 and 40 new stores during each of the next several years thereafter.

Improve Productivity and Efficiency. We seek to drive productivity through strong comparable store sales performance and by improving operational efficiencies. We expect sales growth will be driven by our investment in our proprietary brands, targeted marketing campaigns and more efficient sales and inventory planning and forecasting, as well as favorable industry trends. In addition, we continue to build on what we believe is our strong track record of consistent store-level execution.

Build on Our Core Strengths. We attribute our success to our focus on and our ability to deliver on our value proposition to the customer, which results from leveraging our strength as a vertically-integrated, low-cost operator. As we continue to increase our revenues by opening new stores and marketing our proprietary brands, we also plan to decrease marginal costs by taking advantage of improving economies of scale in purchasing, leveraging our existing infrastructure and other fixed expenses and optimizing our finishing, distribution and supply chain management.

Leverage Our Multi-Channel Sales and Brand Marketing. We use our advertising and marketing activities and our multiple sales channels to help educate potential customers about hardwood flooring. As customers learn more about hardwood flooring and how best to shop for it, they also learn more about our products and value proposition, which we believe drives customer store visits and purchases of our products. We believe that as we continue to leverage our multi-channel strategy, we will drive repeat customer traffic. We have also made a significant advertising and marketing investment to link our brands to quality and value as well as to establish ourselves as the hardwood flooring experts. As we continue to grow and open more stores, we believe that our marketing and branding activities will become more efficient and targeted. We also believe that our customer acquisition costs will decline on both a per-customer and per-store basis.

Our Market

The hardwood flooring market represents approximately 10% of the overall U.S. floor coverings market. Catalina Research Inc. estimates that the value of U.S. hardwood flooring wholesale sales in 2005 was approximately $2.3 billion (representing retail sales of $4.1 billion), and that the market will grow at a compound annual growth rate of 7.4% through 2011. We believe we will continue to benefit from several key long-term industry trends and characteristics including increased home improvement spending (which is driven by several factors including the aging of existing housing stock, increasing home ownership levels, the increasing average size of homes and favorable demographic trends), the evolution of the hardwood flooring market to include both a wider range of wood species and products that are increasingly easier and less costly to install, and the greater attractiveness of hardwood flooring as industry innovations drive growth and its perceived cosmetic, durability and health advantages.

Risk Factors

We face a number of risks in operating our business, including risks that may prevent us from achieving our business objectives or that may affect our business, financial condition and operating results. You should consider these risks before investing in our company. For example:

Dependence on the Economy, Home Remodeling Activity and the Homebuilding Industry. Our industry is highly dependent on the remodeling of existing homes and new home construction, which depend on factors such as interest rates, tax policy, employment levels, consumer confidence, credit availability, real estate prices, demographic trends, weather conditions, natural disasters and general economic conditions. Market trends or other events that limit discretionary consumer spending, reduce spending on remodeling of existing homes and cause purchases of new homes to decline could adversely affect our operations. For example, Catalina Research, Inc. estimates that U.S. hardwood flooring sales declined by 10.6% in 2006, with a 15.2% decline in square-foot sales in the fourth quarter of 2006, principally as a result of decreased new housing demand.

Unpredictability of Future Results. Our growth strategy, and the investment associated with the development of new stores, may cause our operating results to fluctuate and be unpredictable or decrease our profits. Our future results will depend on factors that include successfully selecting new markets and store locations, negotiating leases on acceptable terms, managing construction, occupancy and operating costs, maintaining the quality of our operations, developing consumer recognition of the quality of our products, meeting customer demand and the continued popularity of hardwood flooring. In addition, as we open more stores, our rate of expansion relative to the size of our store base will decline, newly opened stores may not succeed or may reach profitability more slowly than we expect, and the ramp-up to profitability may become longer in the future.

Managing our Growth Effectively. Our existing management information systems, including our store management systems and financial and management controls, may be unable to support our planned expansion. We will need to continue to enhance these systems, procedures and controls, to hire, train and retain regional managers, store managers and store staff and to integrate newly hired management personnel.

Continued Availability of Sufficient Suitable Hardwood. Some of the hardwood species we sell are scarce, and we cannot be assured of their continued availability. Our ability to obtain an adequate volume and quality of hard-to-find species depends on our suppliers ability to furnish those species, which, in turn, could be affected by events such as forest fires, insect infestation, tree diseases, prolonged drought, other adverse weather conditions, changes in government regulations relating to forest management practices and changes to regulations and forest management policies.

Reliance on and Relationships with Certain Suppliers. Our 10 largest suppliers accounted for approximately 63% of our purchases in 2006, and one supplier represented approximately 14% of our purchases and acted as agent for a second supplier that accounted for another 7%. We generally do not have long-term contracts with our suppliers, and they may be unable to supply us in the future due to various factors. In addition, in order to retain the competitive advantage that we believe results from our direct supplier relationships, we need to continue to identify, develop and maintain relationships with qualified mills that can satisfy our high standards for quality and our requirements for hardwood in a timely and efficient manner.

Increased Hardwood or Delivery Costs. The costs of the species of hardwood that we use in our products and delivery costs (particularly fuel costs) can fluctuate due to various factors, and we may not always be able to increase the selling prices of our products in response to increases in those costs.

We also face a number of other risks relating to various aspects of our business and operations, including the possibility of disruptions to our management information systems, call center or website; our ability to hire and retain qualified officers, managers and employees; increasing competitive pressures; problems potentially arising at our single finishing and distribution center; the continued effectiveness of our advertising and product endorsement strategy; and concentrated shareholder ownership. You should carefully consider the risks discussed in Risk Factors before deciding to invest in our common stock.

Our Corporate History and Principal Office

We were incorporated in Massachusetts in 1994 as Lumber Liquidators, Inc. In connection with this offering, we will become a Delaware corporation. Our corporate and principal executive office is located at 3000 John Deere Road, Toano, Virginia 23168. Our telephone number is (757) 259-4280, and we maintain a website at www.lumberliquidators.com on which we will post all reports we file with the Securities and Exchange Commission, or the SEC, under Section 13(a) of the Securities Exchange Act of 1934 after the closing of this offering. We also will post on this site our key corporate governance documents, including our board committee charters, our ethics policy and our principles of corporate governance. We also offer information about our premium Bellawood brand on a separate website at www.bellawood.com and about the Ty Pennington collection at www.tyscollection.com. Information on these websites is not, however, a part of this prospectus.

Sources of Market and Industry Data

This prospectus includes market share and industry data and forecasts that we have obtained from internal company surveys, market research, consultant surveys, publicly available information and industry publications and surveys. Information regarding the hardwood flooring market is derived from Catalina Research Inc. s *November 2005 Wood Flooring Report* and *March 2007 Floor Coverings Industry Quarterly Update* and other sources identified herein. Information regarding our market position has been derived in part from information in *Floor Covering Weekly* and *Floor Focus* magazines. Except where otherwise noted, statements as to our position relative to our competitors or as to market share refer to the most recent available data.

Use of Trademarks and Trade Names

We have a number of registered marks, including Lumber Liquidators®, Bellawood®, 1-800-FLOORING®, the Lumber Liquidators design mark and others, in several jurisdictions including the United States, and we have also applied to register a number of other marks in various jurisdictions. See Business Intellectual Property and Trademarks. This prospectus also contains trademarks and trade names of other companies. All trademarks and trade names appearing in this prospectus are the property of their respective holders.

Table of Contents

The Offering

Common stock offered by us	Shares
Common stock offered by the selling stockholders	Shares
Common stock to be outstanding after this offering	Shares
Use of proceeds	We estimate that the net proceeds to us from this offering will be approximately $ million (based on the midpoint of the range shown on the cover page of this prospectus). We will not receive any proceeds from the sale of shares by the selling stockholders. The selling stockholders include the chairman of our board of directors. See Use of Proceeds for more information. We intend to repay all amounts outstanding under our senior secured loan agreement (approximately $10.8 million as of May 31, 2007) using proceeds from this offering. We intend to use the remainder of the net proceeds of this offering to provide additional long-term capital to support the growth of our business and for general corporate purposes.
Dividends	We do not anticipate paying any cash dividends in the foreseeable future.
Proposed New York Stock Exchange symbol	LL
Risk Factors	See Risk Factors beginning on page 9 and other information included in this prospectus for a discussion of factors that you should carefully consider before investing in our common stock.

The number of shares of common stock that will be outstanding after this offering in the table above excludes:

- shares of common stock issuable upon exercise of outstanding stock options with a weighted average exercise price of $ per share, of which were vested as of , 2007.

Except as otherwise noted, all information in this prospectus:

- reflects a for one split of our common stock in the form of a stock dividend to be effected prior to the consummation of this offering;
- assumes that the underwriters do not exercise their option to purchase up to additional shares of common stock from the selling stockholders;
- gives effect to the conversion of 7,952,018 shares of series A convertible preferred stock held by TA Associates that were outstanding prior to this offering into shares of common stock;
- excludes restricted stock grants of shares of common stock that we intend to grant to certain executive officers and employees at the closing of the initial public offering; and

excludes stock option grants that we intend to grant certain directors on the day this offering is priced for sale to the public to purchase shares of common stock at the initial public offering price.

Table of Contents

Summary Financial Data

You should read the data set forth below in conjunction with our financial statements and related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations, Unaudited Pro Forma Financial Information and other financial information included elsewhere in this prospectus. We derived the summary financial data as of December 31, 2005 and 2006 and for each of the years ended December 31, 2004, 2005 and 2006 from our audited financial statements and the related notes appearing elsewhere in this prospectus. We derived the summary financial data as of December 31, 2004 from our audited financial statements and the related notes not included in this prospectus. We derived the summary financial data as of and for the years ended December 31, 2002 and 2003 from our unaudited financial statements not included in this prospectus. The summary statements of income data for the three months ended March 31, 2006 and 2007 and the summary balance sheet data as of March 31, 2007 have been derived from our unaudited financial statements appearing elsewhere in this prospectus which, in the opinion of our management, have been prepared on the same basis as the audited financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of our operating results and financial position for those periods and as of those dates. The summary unaudited financial data for the three months ended March 31, 2007 are not necessarily indicative of our results for the year ending December 31, 2007 and our historical results are not necessarily indicative of our results for any future period.

	Year Ended December 31,					Three Months Ended March 31,	
	2002	2003	2004	2005	2006(1)	2006(1)	2007(1)
	(in thousands, except share and per share amounts)						
	(unaudited)	(unaudited)				(unaudited)	(unaudited)
Statement of Income Data							
Net sales	$ 65,382	$ 100,866	$ 171,766	$ 244,947	$ 332,060	$ 76,051	$ 92,022
Cost of sales	43,051	67,870	115,857	158,844	221,931	49,642	61,451
Gross profit	22,331	32,996	55,909	86,103	110,129	26,409	30,571
Selling, general and administrative expenses	17,545	29,566	48,461	67,900	88,716	20,537	26,816
Impairment loss on long-lived assets		955	293				
Operating income	4,786	2,475	7,155	18,203	21,413	5,872	3,755
Interest expense	160	218	429	638	722	167	174
Other (income) expense(2)	(318)	(428)	190	(96)	(368)	(107)	(55)
Income before income taxes	4,944	2,685	6,536	17,661	21,059	5,812	3,636
Provision for income taxes(3)	163	65	(1,450)	6,948	8,161	2,252	1,405
Net income	$ 4,781	$ 2,620	$ 7,986	$ 10,713	$ 12,898	$ 3,560	$ 2,231
Net income per common share:							
Basic	$ 0.32	$ 0.17	$ 0.53	$ 0.71	$ 0.86	$ 0.24	$ 0.15
Diluted	$ 0.32	$ 0.17	$ 0.51	$ 0.46	$ 0.56	$ 0.15	$ 0.10
Weighted average common shares outstanding(4):							

Basic	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100
Diluted	15,000,100	15,000,100	15,675,477	23,063,174	22,989,403	23,037,415	22,952,118
Pro Forma Income Statement Data(5):							
Pro forma net income					$		$
Pro forma net income per common share:							
Basic					$		$
Diluted					$		$
Pro forma weighted average common shares outstanding:							
Basic							
Diluted							

Table of Contents

(1) We adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (R), *Share-Based Payment* (SFAS No. 123(R)), using the prospective-transition method, effective January 1, 2006.
(2) Includes interest income.
(3) Effective December 1, 2004, we elected to be taxed as a C corporation for federal and state income tax purposes. Prior to this election, we were not subject to federal or certain state income taxation at the corporation level.
(4) Share amounts as of December 31, 2002 and 2003 have been adjusted to reflect the December 2004 common stock dividend of 150,000:1 to Tom Sullivan, our founder and chairman of our board of directors.
(5) The pro forma statement of income data for the year ended December 31, 2006 and three months ended March 31, 2007 were derived from our Unaudited Pro Forma Financial Information included elsewhere in this prospectus.

	As of December 31, (in thousands)					As of March 31,
	2002	2003	2004	2005	2006	2007
	(unaudited)	(unaudited)				(unaudited)
Balance Sheet Data						
Cash and cash equivalents	$ 384	$ 3,073	$ 3,031	$ 6,031	$ 3,965	$ 5,145
Merchandise inventories	9,501	14,910	22,507	30,009	51,758	63,472
Total assets	13,249	21,017	39,753	55,162	78,020	75,105
Total debt and capital lease obligations, including current maturities	2,555	2,617	12,364	10,360	9,603	8,284
Stock compensation liability	850	2,020	4,958	8,092	9,132	9,534
Redeemable preferred stock			34,693	34,744	34,795	34,808
Total stockholder s equity (deficit)	4,260	3,620	(30,242)	(18,775)	(5,468)	(2,814)
Working capital(1)	4,299	5,230	8,091	17,059	29,697	22,107
Pro Forma Balance Sheet Data(2):						
Pro forma cash and cash equivalents						$
Pro forma total debt and capital lease obligations, including current maturities						$
Pro forma stock compensation liability						$
Pro forma redeemable preferred stock						$
Pro forma total stockholders equity (deficit)						$

(1) Working capital is defined as current assets minus current liabilities.

(2) The pro forma balance sheet data as of March 31, 2007 were derived from our Unaudited Pro Forma Financial Information included elsewhere in this prospectus.

	Year Ended December 31, (in thousands, except % and numbers of stores)					Three Months Ended March 31,	
	2002	2003	2004	2005	2006	2006	2007
Operating Data							
Number of stores open at end of period	25	40	57	76	91	80	93
Comparable store sales increase(1)(2)	NA	22.9%	38.2%	19.0%	17.3%	24.1%	8.5%
Depreciation and amortization	$ 1,033	$ 883	$ 1,157	$ 2,240	$ 2,908	$ 611	$ 869

Capital expenditures:							
New store openings	$ 22	$ 112	$ 225	$ 352	$ 225	$ 51	$ 88
Other(3)	371	410	6,322	3,975	2,494	503	756
Total capital expenditures	$ 393	$ 522	$ 6,547	$ 4,327	$ 2,719	554	844

(1) Stores are considered comparable on the first day of the thirteenth full calendar month of operation.
(2) Comparable store sales data is not available for the year ended December 31, 2002 on the same basis as for subsequent periods.
(3) Consists primarily of expenditures on expenses related to establishing our Toano facility (which opened in 2004), purchases of trailers, leasehold improvements, information technology and warehouse equipment.

Table of Contents

RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the following information about these risks, together with the other information contained in this prospectus, before deciding to buy our common stock. Any of the risks we describe below could adversely affect our business, financial condition or operating results. The market price of our common stock could decline if one or more of these risks and uncertainties develop into actual events. You could lose all or part of your investment.

Risks Related to Our Business and Industry

The hardwood flooring industry depends on the economy, home remodeling activity, the homebuilding industry and other important factors.

The hardwood flooring industry is highly dependent on the remodeling of existing homes and new home construction. In turn, remodeling and new home construction depend on a number of factors which are beyond our control, including interest rates, tax policy, employment levels, consumer confidence, credit availability, real estate prices, demographic trends, weather conditions, natural disasters and general economic conditions. If:

- the national economy or any regional or local economy where we operate weakens;
- interest rates rise;
- credit becomes less available;
- regions where we operate experience unfavorable demographic trends;
- fuel costs or utility expenses increase; or
- home-price appreciation slows;

that could limit discretionary consumer spending, reduce spending on remodeling of existing homes and cause purchases of new homes to decline. For example, although our net sales increased during 2006, Catalina Research Inc. estimates that U.S. hardwood flooring sales declined by 10.6% in 2006, with a 15.2% decline in square-foot sales in the fourth quarter of 2006, principally as a result of decreased new housing demand. Any one or a combination of these factors could result in decreased demand for hard surface flooring, including in particular premium hardwood flooring, in remodeled and new homes, which would harm our business and operating results.

The planned rapid increase in the number of our stores may make our future results unpredictable.

As of May 31, 2007, we had 98 stores throughout the United States, 74 of which we opened after January 1, 2003. We plan to open 25 stores in 2007 and between 30 and 40 new stores during each of the next several years thereafter. This growth strategy and the investment associated with the development of each new store may cause our operating results to fluctuate and be unpredictable or decrease our profits. Our future results will depend on various factors, including the successful selection of new markets and store locations, our ability to negotiate leases on acceptable terms, management of pre-opening expenses, the quality of our operations, consumer recognition of the quality of our products, our ability to meet customer demand, the continued popularity of hardwood flooring and general economic conditions. In addition, as we open more stores, our rate of expansion relative to the size of our store base will decline. We may not be able to identify suitable store locations in markets into which we seek to expand and may not be able to open as many stores as planned. Consumers in a new market may be less familiar with our brands, and we may need to increase brand awareness in that market through additional investments in advertising. Stores opened in new markets may have higher construction, occupancy or operating costs, or may have lower average store sales, than stores opened in the past. In addition, we may incur higher maintenance costs associated with our strategy of seeking out low-cost store locations than in the past. Newly opened stores may not succeed or may reach profitability more slowly than we expect, and the ramp-up to profitability may become longer in the future as we enter more mid-sized and smaller markets and add stores to larger markets where we already have a presence. Future markets and stores may not be successful and, even if we are successful, our average store sales and our comparable store sales may not increase at historical rates.

Failure to manage our growth effectively could harm our business and operating results.

Our plans call for a significant number of new stores, and increased sales from our website, call center and catalog. Our existing management information systems, including our store management systems and financial and management controls, may be unable to support our expansion. Managing our growth effectively will require us to continue to enhance these systems, procedures and controls and to hire, train and retain regional managers, store managers and store staff. In addition, we have hired a number of senior managers in 2006 and 2007, and execution of our strategy requires that they be integrated effectively. We may not respond quickly enough to the changing demands that our expansion will impose on our management, staff and existing infrastructure. Any failure to manage our growth effectively could harm our business and operating results.

Our ability to produce hardwood flooring, particularly products made of more exotic species, depends on the continued availability of sufficient suitable hardwood.

Our business strategy depends on offering a wide assortment of hardwood flooring to our customers. We sell flooring made from species ranging from domestic maple, oak and pine to imported cherry, ebony, mahogany and teak. Some of these species are scarce, and we cannot be assured of their continued availability, especially of exotic hardwoods that comprise a significant portion of our more profitable products. Our ability to obtain an adequate volume and quality of hard-to-find species depends on our suppliers ability to furnish those species, which, in turn, could be affected by many things including events such as forest fires, insect infestation, tree diseases, prolonged drought and other adverse weather conditions. Government regulations relating to forest management practices also affect our suppliers ability to harvest or export timber, and changes to regulations and forest management policies, or the implementation of new laws or regulations, could impede their ability to do so. If our suppliers cannot deliver sufficient hardwood and we cannot find replacement suppliers, we would need to curtail finishing of the relevant product lines, which could cause our operating results to deteriorate.

Our dependence on certain suppliers makes us vulnerable to the extent we rely on them.

We rely on a concentrated number of suppliers for the majority of our supply needs. In 2006, one of our suppliers, Sequoia Floorings, accounted for approximately 14% of our purchases, and acted as agent for another of our suppliers, EPI, which accounted for another 7% of our purchases. Including those companies, our top 10 suppliers account for approximately 63% of our purchases in 2006. We generally do not have long-term contracts with our suppliers, and we typically obtain our hardwood supplies on an order-by-order basis, writing orders for future deliveries from 90 to 180 days before delivery. Our suppliers may be unable to supply us in the future due to various factors, which could include political instability in the supplier s country, a supplier s financial instability, inability or refusal to comply with applicable laws, trade restrictions or tariffs, insufficient transport capacity and other factors beyond our control. If we can no longer obtain merchandise from our major suppliers, or they refuse to continue to supply us on commercially reasonable terms or at all, and we cannot find replacement suppliers, we could experience a deterioration in our sales and operating results.

Table of Contents

If we fail to identify and develop relationships with a sufficient number of qualified mills, our ability to obtain hardwood products that meet our high quality standards could be harmed.

We purchase flooring directly from mills located around the world. We believe that these direct supplier relationships are relatively unique in our industry. In order to retain the competitive advantage that we believe results from these relationships, we need to continue to identify, develop and maintain relationships with qualified mills that can satisfy our high standards for quality and our requirements for hardwood in a timely and efficient manner. The need to develop new relationships will be particularly important as we seek to expand our operations in the future. Any inability to do so could reduce our competitiveness, slow our plans for further expansion and cause our sales and operating results to deteriorate.

Our ability to obtain hardwood from abroad and the operations of many of our international suppliers are subject to risks that are beyond our control and that could harm our operations.

We rely on a select group of international suppliers to provide us with hardwood products that meet our specifications. In 2006, approximately 30% of our product was sourced from Asia, approximately 24% was sourced from South America and approximately 11% was sourced from other locations outside of North America. As a result, we are subject to risks associated with obtaining products from abroad, including:

- political unrest, terrorism and economic instability resulting in the disruption of trade from foreign countries where our products originate;
- currency exchange fluctuations;
- the imposition of new laws and regulations, including those relating to environmental matters; imports, duties, taxes and other charges on exports or imports; labor conditions; quality and safety standards; trade restrictions; and restrictions on funds transfers;
- disruptions or delays in shipments; and
- changes in local economic conditions in countries where our suppliers are located.

These and other factors beyond our control could disrupt the ability of our suppliers to ship certain products to us cost-effectively or at all, which could harm our operations.

Increased hardwood costs could harm our results of operations.

The cost of the various species of hardwood that we use in our products is important to our profitability. Hardwood lumber costs fluctuate because of changes in domestic and international supply and demand, labor costs, competition, market speculation, product availability, environmental restrictions, government regulation and trade policies, weather conditions, processing and freight costs and delivery delays. We generally do not have long-term supply contracts or guaranteed purchase amounts. As a result, we may not be able to anticipate or react to changing hardwood costs by adjusting our purchasing practices, and we may not always be able to increase the selling prices of our products in response to increases in supply costs. If we cannot address changing hardwood costs appropriately, it could cause our operating results to deteriorate.

Increased delivery costs, particularly those relating to the cost of fuel, could harm our results of operations.

We source merchandise from around the world, and our cost of sales includes the cost of delivery to our Toano facility. In addition, we rely on third-party trucking companies to transport our products from our Toano facility to our stores and from our stores to our customers. If the cost of fuel or other

costs, such as import tariffs, rise, it could result in increases in our cost of sales and selling, general and administrative expenses due to additional delivery charges and in the fees transportation companies charge us to transport our products to our stores and customers. We may be unable to increase the price of our products to offset increased delivery charges, which could cause our operating results to deteriorate.

If our management information systems experience disruptions, it could disrupt our business and reduce our sales.

We depend on our management information systems to integrate the activities of our stores, website and call center, to process orders, to respond to customer inquiries, to manage inventory, to purchase merchandise and to sell and ship goods on a timely basis. Our high growth rate creates additional challenges in maintaining and expanding our systems. We may experience operational problems with our information systems as a result of system failures, viruses, computer hackers or other causes. We have identified improvements that we need to make to our internal controls that relate to limiting access to our information systems, which we expect to implement over the next 18 months. Any significant disruption or slowdown of our systems, including a disruption or slowdown caused by our failure to successfully upgrade our systems, could cause information, including data related to customer orders, to be lost or delayed, which could result in delays in the delivery of products to our stores and customers or lost sales. During 2007, we are introducing two new management information systems:

- In the first quarter of 2007, we upgraded our entire corporate network, including our telephone lines, to an Internet-based network. If our network is disrupted, we may experience delayed communications within our operations and between our customers and ourselves, and may not be able to communicate at all via our network, including via telephones connected to our network.

- Before the end of 2007, we plan to introduce a new point-of-sale system to improve the tracking of inventory and sales information in all of our stores. If the introduction of this system interferes with our existing system, we could experience disruptions in our ability to stock our stores and fulfill customer orders in a timely manner.

Moreover, we may in the future be unable to develop or acquire technology that meets our needs or those of our customers, or have insufficient resources to make necessary investments in technology. Accordingly, if our information systems are inadequate to handle our growth or if changes in technology cause our information systems to become obsolete, it could disrupt or otherwise harm our operations.

Any disruption of our website or our call center could disrupt our business and lead to reduced sales and reputational damage.

Our website and our call center are integral parts of our integrated multi-channel strategy. Customers use our website and our call center as information sources on the range of products available to them and to order our products, samples or catalogs. Our website in particular is vulnerable to certain risks and uncertainties associated with the Internet, including changes in required technology interfaces, website downtime and other technical failures, security breaches and consumer privacy concerns. If we cannot successfully maintain our website and call center in good working order, it could reduce our sales and damage our reputation.

Our success depends substantially upon the continued retention of certain key personnel.

We believe that our success has depended and continues to depend to a significant extent on the efforts and abilities of our senior management team and our board of directors. Our failure to retain members of that team could impede our ability to build on the efforts they have undertaken with respect to our business. Specifically, the loss of Tom Sullivan, our founder and the chairman of our board of directors, could harm us. Under his guidance, we experienced rapid growth and established ourselves as a leading company in the industry. Tom continues to have an active role in determining our strategic direction and assisting with our day-to-day operations, and we believe that if we no longer had access to his product knowledge and relationships with our suppliers, it would eliminate an important competitive advantage. In addition, the loss of Jeff Griffiths, our president and chief executive officer, or Dan Terrell, our chief financial officer, could harm us, as we rely on their significant experience with reporting companies and the retail industry.

Our success depends upon our ability to attract, train and retain highly qualified managers and staff.

Our success depends in part on our ability to attract, hire, train and retain qualified managers and staff. Buying hardwood flooring is an infrequent event, and the typical consumer has very little knowledge of the range, characteristics and suitability of the products available to them before starting the purchasing process. Therefore, consumers in the hardwood flooring market expect to have sales associates serving them who are knowledgeable about the entire assortment of products offered by the retailer and the process of choosing and installing hardwood flooring. As a result, competition for qualified store managers and sales associates among flooring retailers is intense. We may not succeed in attracting and retaining the personnel we require to conduct our current operations and support our potential future growth. In addition, as we expand into new markets, we may find it more difficult to hire, motivate and retain qualified employees.

Increased competition could cause price declines, decrease demand for our products and decrease our market share.

We operate in the hardwood flooring industry, which is highly fragmented and competitive. We face significant competition from multinational home improvement chains, national and regional flooring specialty chains, Internet-based companies and privately-owned single-site enterprises. We compete on the basis of price, customer service, store location and range, quality and availability of hardwood flooring we offer our customers. Our competitive position is also influenced by the availability, quality and cost of merchandise, labor costs, finishing, distribution and sales efficiencies and our productivity compared to that of our competitors. As we expand into new and unfamiliar markets, we may experience different competitive conditions than in the past.

Some of our competitors are larger organizations, have existed longer, are more diversified in the products they offer and have a more established market presence with substantially greater financial, marketing, personnel and other resources than we have. In addition, our competitors may forecast market developments more accurately than we do, develop products that are superior to ours or produce similar products at a lower cost, or adapt more quickly to new technologies or evolving customer requirements than we do. Intense competitive pressures from one or more of our competitors could cause price declines, decrease demand for our products and decrease our market share.

Hardwood flooring may become less popular as compared to other types of floor coverings in the future. For example, our products are made using various hardwood species, including rare exotic hardwood species harvested from rainforests, and concern over the environmental impact of tree harvesting could shift consumer preference towards synthetic or inorganic flooring. In addition, hardwood flooring competes against carpet, vinyl sheet, vinyl tile, ceramic tile, natural stone and other types of floor coverings. If consumer preferences shift towards types of floor coverings other than hardwood flooring, we may experience decreased demand for our products.

All of these competitive factors may harm us and reduce our sales and profits.

Damage, destruction or disruption of our Toano finishing and distribution facility could significantly impede our ability to finish and distribute our products.

We currently finish 75% of all Bellawood products at our Toano finishing facility. In 2006, Bellawood flooring accounted for approximately one-third of our net sales. We also finish small quantities of certain of our other products there. The Toano facility also serves as our distribution center, and approximately 85% of our merchandise passes through this facility before we move it to our stores. The Toano facility also houses our primary computer systems, which control our management information and inventory management systems, and our corporate headquarters. We do not have any other finishing or distribution facilities. If the Toano facility or our inventory held there were damaged or destroyed by fire, wood infestation or other causes, our entire finishing and distribution processes would be disrupted, which could cause significant lost production and delays in delivery. This could impede our ability to stock our stores and deliver products to our customers, and cause our sales and operating results to deteriorate.

Failure to maintain relevant product endorsement agreements and product placement arrangements could harm our reputation and cause our sales to deteriorate.

We have established relationships with well-known and respected home improvement celebrities to evaluate, promote and help establish with consumers the high-quality nature of our products. If these individuals were to stop promoting our products, if we were unable to renew our endorsement contracts with them or if we could not find other endorsers of a similar caliber, our sales and reputation could be harmed. Similarly, any actions that persons endorsing our products may take, whether or not associated with our products, which harm their or our reputations could also harm our brand image with consumers and our reputation, and cause our sales to deteriorate. We also have a number of product placement arrangements with home improvement-related television shows. We rely on these arrangements to increase awareness of our brands, and to enable potential customers to see both what our flooring will look like after installation and the relative ease with which it can be installed. Any failure to continue these arrangements could cause our brands to become less well-known and cause our sales to deteriorate.

Our success depends on the continued effectiveness of our advertising strategy.

We believe that our past success was achieved in part through our successful investment in local and national advertising. We typically locate our stores in industrial or commercial areas that have lower rents than traditional retail locations, but that are generally set some distance from population centers and downtown urban areas. To support this real estate strategy, we have used extensive advertising to encourage customers to drive to our stores. We may need to increase our advertising expense to support our business strategy in the future. In addition, we lease but do not own the rights to 1-800-FLOORING. Although we have an indefinite renewal right under the related contract, it could be terminated in certain circumstances, which could increase our costs until we were able to publicize a new toll-free number. If our advertisements fail to draw customers in the future, or if the cost of advertising or other marketing materials increases significantly, we could experience declines in our sales and operating results.

We have entered into a number of lease agreements with a company controlled by our controlling shareholder, which may make it more difficult to modify or terminate those leases.

We have entered into several agreements with related parties in connection with a significant number of transactions, including leases for our Toano facility, which includes a store location, and 26 of our other store locations as of May 31, 2007. Tom Sullivan is the sole owner of ANO LLC, with which we have in the past entered into most such agreements. In addition, Tom is the sole owner of DORA Real Estate Company, LLC and Wood on Wood Road, Inc., and has a 50% membership interest in BMT Holdings, LLC, and we lease one store location from each of these entities. While we believe that these

Table of Contents

leases we have signed to date are on fair market terms and that the shareholders agreement to which Tom and TA Associates are parties prevents entities affiliated with Tom from setting lease rates above market rates, it may be more difficult for us to modify or terminate those leases in the future, or we may be prevented from doing so by the actions of Tom, who will continue to be a significant shareholder following this offering. See Certain Relationships and Related Party Transactions Store Lease Arrangements.

We will incur non-cash compensation expenses, and may be required to issue shares of common stock, in connection with existing stock-based compensation agreements.

In connection with this offering, Kevin Sullivan, Tom s brother, who started our western U.S. operations and was our first regional manager, will receive shares of our common stock, to be contributed by Tom and which have been placed in escrow, pursuant to an agreement between Tom and Kevin that we have guaranteed. The number of shares to be delivered depends upon a calculation of the value of our western U.S. sales region. While the agreement provides that the number of shares will be fixed in connection with this offering, if the parties disagree on the calculation, the number of shares may need to be adjusted in the future, which could require us to record an additional non-cash stock compensation liability expense. We do not know what the magnitude would be of any such future non-cash compensation expense. We recorded a non-cash compensation expense relating to this matter of $0.4 million in the first quarter of 2007, $1.0 million in 2006, $3.1 million in 2005 and $2.9 million in 2004, and as of March 31, 2007 carried a short-term liability of $9.5 million on our balance sheet relating to this agreement.

We have also received a demand letter from counsel representing a former senior executive in connection with his resignation of employment. That executive alleges that he terminated his employment for good reason, as defined in his employment agreement and our warrant plan which, under the provisions of our warrant plan, could entitle him to shares in an amount equal to up to 1.0% of our outstanding common stock. Although the former executive has not filed a lawsuit or a demand for arbitration, we could be required to issue additional shares of stock in connection with any such action if we were found to be liable for those obligations.

We may not be able to adequately protect our intellectual property, which could harm the value of our brands and harm our business.

Our intellectual property is material to the conduct of our business. Our ability to implement our business plan successfully depends in part on our ability to further build brand recognition using our trademarks, service marks and other proprietary intellectual property, including our name and logo and the names of our brands. If our efforts to protect our intellectual property are inadequate, or if any third party infringes on or misappropriates our intellectual property, either in print or on the Internet, the value of our brands may be harmed, which could adversely affect our business and might prevent our brands from achieving or maintaining market acceptance. We may also encounter claims from prior users of similar intellectual property in locales where we operate or intend to operate. This could harm our image, brand or competitive position and cause us to incur significant penalties and costs.

Environmental, health and safety laws and regulations could increase the cost of doing business or restrict our ability to conduct our business.

We are subject to a wide range of general and industry-specific environmental, health and safety and other laws and regulations imposed by federal, state and local authorities, including those governing the use, storage, handling, generation, treatment, emission, release, discharge and disposal of certain hazardous materials and wastes, the remediation of contaminated soil and groundwater and the health and safety of employees. If we are unable to extend or renew a material approval, license or permit required by such laws, or if there is a delay in renewing any material approval, license or permit, that may cause our sales and operating results to deteriorate or otherwise harm our business.

We will incur increased costs and be required to carry out activities we have not previously undertaken as a result of becoming a public company.

As a public company, we will incur significant legal, accounting and other expenses that we did not incur as a private company. The Sarbanes-Oxley Act of 2002 and related rules of the SEC and the New York Stock Exchange regulate corporate governance practices of public companies. Complying with these requirements will likely increase our costs and make some activities more time-consuming. For example, we will need to adopt new internal controls and disclosure controls and procedures and create new board committees, and also expect to modify director compensation and possibly to increase the number of directors. We will also incur additional expenses associated with our SEC reporting requirements. A number of those requirements will require us to carry out activities we have not previously undertaken. For example, under Section 404 of the Sarbanes-Oxley Act, for our annual report on Form 10-K for 2008 we will need to document and test our internal control procedures, our management will need to assess and report on our internal control over financial reporting and our independent registered public accounting firm will need to issue an opinion on that assessment and the effectiveness of those controls. If we identify any issues in complying with those requirements (for example, if a material weakness was identified in our internal control over financial reporting), we could also incur additional costs rectifying those issues, and their existence could impact our reputation or investor perceptions of us or otherwise harm our business. We are currently not aware of any material weaknesses in our internal controls or disclosure controls. In addition, we expect that it will be difficult and expensive to obtain director and officer liability insurance. As a result, it may be more difficult for us to attract and retain qualified persons to serve on our board of directors or as executive officers. Advocacy efforts by shareholders and third parties may also prompt even more changes in governance and reporting requirements. We cannot predict or estimate the amount of additional costs we may incur or the timing of such costs.

Risks Relating to Our Common Stock and This Offering

There is no existing market for our common stock and we do not know if one will develop. Even if a market does develop, the stock prices in the market may not exceed the offering price.

Prior to this initial public offering, there has not been a public market for our common stock. We cannot predict the extent to which investor interest in our company will lead to the development of an active trading market on the New York Stock Exchange or otherwise, or how liquid that market may become. If an active trading market does not develop, you may have difficulty selling any shares that you buy. In addition, the initial public offering price for the common stock was determined by negotiations between us and the representatives of the underwriters and may not be indicative of prices that will prevail in the open market following this offering. Consequently, you may not be able to sell shares of our common stock at prices equal to or greater than the price you pay in this offering.

Tom Sullivan and TA Associates will have the ability to exercise significant influence over us after this offering, and their interests in our business may be different than yours.

All of the issued and outstanding shares of our common stock are currently owned by Tom Sullivan, while TA Associates indirectly beneficially owns all of our outstanding series A convertible preferred stock. Assuming that TA Associates converts all of its preferred stock into common stock and that the underwriters do not exercise their option to purchase additional shares, upon completion of this offering, Tom will control approximately %, and TA Associates will control approximately %, of our outstanding common stock, which also reflects the transfer of an estimated million shares from Tom to Kevin Sullivan pursuant to an equity compensation agreement. Accordingly, each of these parties

Table of Contents

will be able to exercise significant influence over our business policies and affairs and all matters requiring a stockholders vote, including the composition of our board of directors, the adoption of amendments to our certificate of incorporation and the approval of mergers or sales of all or substantially all of our assets. This concentration of ownership could also delay, defer or even prevent a change in control of our company and may make some transactions more difficult or impossible without their support. These interests of these stockholders may conflict with yours, and they may seek to cause us to take courses of action that, in their judgment, could enhance their investment in us, but which might involve risks to holders of our common stock or be harmful to our business or other investors.

Our anti-takeover defense provisions may cause our common stock to trade at market prices lower than it might absent such provisions.

Our new certificate of incorporation and bylaws will contain several provisions that may make it more difficult or expensive for a third party to acquire control of us without the approval of our board of directors. These provisions include a staggered board, the availability of blank check preferred stock, provisions restricting stockholders from calling a special meeting of stockholders or requiring one to be called or from taking action by written consent and provisions that set forth advance notice procedures for stockholders nominations of directors and proposals of topics for consideration at meetings of stockholders. Our certificate of incorporation will also provide that Section 203 of the Delaware General Corporation Law, which relates to business combinations with interested stockholders, will apply to us. These provisions may delay, prevent or deter a merger, acquisition, tender offer, proxy contest or other transaction that might otherwise result in our shareholders receiving a premium over the market price for their common stock. In addition, these provisions may cause our common stock to trade at a market price lower than it might absent such provisions.

Our common stock price may be volatile and you may lose all or part of your investment.

The market price of our common stock could fluctuate significantly, and you may not be able to resell your shares at or above the offering price. Those fluctuations could be based on various factors in addition to those otherwise described in this prospectus, including:

- our operating performance and the performance of our competitors;
- the public s reaction to our press releases, our other public announcements and our filings with the SEC;
- changes in earnings estimates or recommendations by research analysts who follow Lumber Liquidators or other companies in our industry;
- variations in general economic conditions;
- the number of shares to be publicly traded after this offering;
- actions of our current shareholders, including sales of common stock by our directors and executive officers;
- the arrival or departure of key personnel; and
- other developments affecting us, our industry or our competitors.

In addition, in recent years the stock market has experienced significant price and volume fluctuations. These fluctuations may be unrelated to the operating performance of particular companies but may cause declines in the market price of our common stock. The price of our common stock could fluctuate based upon factors that have little or nothing to do with our company or its performance.

Table of Contents

Purchasers in this offering will experience immediate and substantial dilution.

Prior investors have paid substantially less per share than the price in this offering. The initial public offering price is substantially higher than the net tangible book value per share of the outstanding common stock immediately upon completion of this offering. As a result, investors purchasing our common stock in this offering will incur immediate dilution of $ per share. The exercise of outstanding options and future equity issuances at prices below the initial public offering price would result in further dilution to purchasers in this offering.

Future sales of our common stock, or the perception that such sales may occur, could cause our stock price to fall.

Sales of substantial amounts of our common stock in the public market after the consummation of this offering, or the perception that such sales may occur, could harm the market price of our common stock and could materially impair our ability to raise capital in the future through offerings of our common stock.

We, our executive officers and directors and the selling stockholders have agreed, subject to certain exceptions, not to dispose of or hedge any common stock or securities convertible into or exchangeable for shares of common stock during the period from the date of this prospectus continuing through the date 180 days after the date of this prospectus, except, in our case, for the issuance of common stock upon exercise of options outstanding under existing option plans. Goldman, Sachs & Co. and Merrill Lynch, Pierce, Fenner & Smith Incorporated may, in their sole discretion, release any of these shares from these restrictions at any time without notice.

All of our shares of common stock outstanding as of the date of this prospectus may be sold in the public market by existing stockholders 180 days after the date of this prospectus, subject to applicable volume and other limitations imposed under federal securities laws. See Shares Eligible for Future Sale for a more detailed description of the restrictions on selling shares of our common stock upon completion of this offering.

We do not intend to pay dividends for the foreseeable future.

For the foreseeable future, we intend to retain any earnings to finance the development and expansion of our business, and we do not anticipate paying any cash dividends on our common stock. Accordingly, investors must be prepared to rely on sales of their common stock after price appreciation to earn an investment return, which may never occur. Investors seeking cash dividends should not purchase our common stock. Any determination to pay dividends in the future will be made at the discretion of our board of directors and will depend on our results of operations, financial condition, contractual restrictions, restrictions imposed by applicable law and other factors our board deems relevant. See Dividend Policy.

Table of Contents

FORWARD-LOOKING STATEMENTS

Some of the statements contained in this prospectus constitute forward-looking statements. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts, such as statements regarding our future financial condition or results of operations, our prospects and strategies for future growth, the development and introduction of new products, and the implementation of our marketing and branding strategies. In many cases, you can identify forward-looking statements by terms such as may, will, should, expects, plans, anticipates, believes, estimates, predicts, potential or the negative of these terms or other comparable terr

The forward-looking statements contained in this prospectus reflect our current views about future events and are subject to risks, uncertainties, assumptions and changes in circumstances that may cause events or our actual activities or results to differ significantly from those expressed in any forward-looking statement. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future events, results, actions, levels of activity, performance or achievements. Readers are cautioned not to place undue reliance on these forward-looking statements. A number of important factors could cause actual results to differ materially from those indicated by the forward-looking statements, including, but not limited to, those factors described in Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations. These factors include, without limitation:

- our ability to continue to increase comparable store sales;
- our ability to add new stores;
- our ability to manage our growth effectively;
- our ability to develop and maintain effective internal controls;
- increased competition causing us to reduce the prices of our products or to increase significantly our marketing efforts in order to avoid losing market share;
- changes in consumer preferences or the reduction in demand for hardwood flooring;
- our ability to accurately forecast consumer demand for our products;
- failure of our suppliers to produce or deliver merchandise to us in a timely or cost-effective manner;
- our ability to accurately anticipate and respond to seasonal or quarterly fluctuations in our operating results;
- the availability and effective operation of management information systems and other technology;
- our ability to attract and maintain the services of our senior management and key employees; and

changes in general economic or market conditions, including as a result of political or military unrest or terrorist attacks.

The forward-looking statements contained in this prospectus reflect our views and assumptions only as of the date of this prospectus. We undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events.

Table of Contents

USE OF PROCEEDS

We estimate that the net proceeds to us from our sale of shares of common stock in this offering, after deducting underwriting discounts, commissions and other estimated offering expenses payable by us, will be approximately $ million (based on the midpoint of the range shown on the cover page of this prospectus). We will not receive any proceeds from the sale of shares by the selling stockholders. In addition, we will not participate in the sale of additional shares relating to the underwriters option to purchase additional shares from the selling stockholders. The chairman of our board of directors is selling shares of common stock in this offering. See Principal and Selling Stockholders.

We intend to repay all amounts outstanding under our senior secured loan agreement (approximately $10.8 million as of May 31, 2007) using proceeds from this offering. Both the term loan portion of our senior secured loan agreement, which is scheduled to mature in 2011, and the revolving facility portion of our senior secured loan agreement bear interest at a per annum rate approximately equal to one-month LIBOR plus 0.90%, or 6.2%, as of May 31, 2007. We currently intend to use any future borrowings under the loan agreement for working capital purposes.

After repayment in full of the amounts outstanding under our senior secured loan agreement, we intend to use the remainder of the net proceeds of the offering to provide additional long-term capital to support the growth of our business and for general corporate purposes. The amounts and timing of our actual expenditures will depend on numerous factors, including the status of our expansion efforts; sales, advertising and marketing activities and our need to expand our finishing and distribution facility. Accordingly, our management will have broad discretion in the application of the net proceeds, and investors will be relying on the judgment of our management regarding the application of the proceeds from this offering.

A $1 change, up or down, in the midpoint of the range shown on the cover page of this prospectus would change our estimated net proceeds by $ million. Similarly, a change in the number of shares of common stock we sell would increase or decrease our net proceeds. We believe that our intended use of proceeds would not be affected by changes in either our initial public offering price or the number of shares of common stock we sell.

DIVIDEND POLICY

We currently anticipate that we will retain any future earnings for use in our business. As a result, we do not anticipate paying any cash dividends in the foreseeable future.

In connection with our sale of shares of our series A convertible preferred stock to TA Associates in December 2004, we implemented a 150,000 to 1 stock split relating to our common stock, which we effected by means of a stock dividend to our sole shareholder, Tom Sullivan, our founder and chairman of our board of directors. The stock split was effected prior to the transaction in order to increase the number of common shares held by Tom from 100 to approximately 15.0 million. The stock split was effected in order to ensure that Tom would continue to hold an appropriate percentage of our common stock upon conversion of the convertible preferred stock held by TA Associates, and the extent of the split was determined in connection with the sale of shares of preferred stock (which is convertible into common stock on a one-to-one basis). We distributed 15,000,000 shares to Tom in connection with the stock split. We also distributed $42.6 million in cash to Tom in 2004, including $30.0 million of the proceeds from the sale of the convertible preferred stock (which represented a significant dilution of his ownership interest), $5.0 million to enable him to pay taxes on deemed income during the period we were an S corporation and $7.6 million of additional cash. We retained cash not distributed to Tom from the sale of our series A convertible preferred stock to provide us with sufficient capital for operating liquidity. Tom, as our sole shareholder and sole director, approved both the stock split and the cash distributions.

Table of Contents

CAPITALIZATION

The following table sets forth our capitalization as of March 31, 2007 on both an actual basis and on a pro forma basis to reflect:

- the sale by us of common stock in this offering, based on an assumed initial public offering price of $ per share (the midpoint of the range shown on the cover page of this prospectus) and after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us;
- the repayment of all amounts outstanding under our senior secured loan agreement (approximately $7.9 million as of March 31, 2007);
- the conversion of 7,952,018 shares of series A convertible preferred stock held by TA Associates that were outstanding prior to this offering into shares of common stock;
- the grant of shares of restricted common stock to certain executive officers and employees, reflecting shares that we intend to grant to such persons at the closing of the initial public offering;
- the expected satisfaction of the stock compensation liability associated with the variable performance equity agreement between Tom Sullivan and Kevin Sullivan, which includes a guarantee by us, through the transfer of shares of common stock from Tom to Kevin; and
- the non-cash compensation expense associated with the regional manager stock unit plan and acceleration of non-cash compensation expense under the 2004 and 2006 stock option plans.

You should read this table in conjunction with the sections of this prospectus captioned Use of Proceeds, Selected Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and Unaudited Pro Forma Financial Information as well as the audited financial statements and related notes included elsewhere in this prospectus.

	As of March 31, 2007		
	Actual		Pro Forma
	(in millions, except share amounts)		
Cash and cash equivalents	$	5.1	
Total debt and capital lease obligations, including current maturities	$	8.3	
Redeemable preferred stock		34.8	
Stockholders equity (deficit):			
Common stock, no par value, 35,000,000 shares authorized, 15,000,100 issued and outstanding; shares authorized, issued and outstanding, pro forma			
Additional capital		1.7	
Retained earnings (deficit)		(4.5)	
Total stockholders equity (deficit)		(2.8)	
Total capitalization	$	40.3	

22

Table of Contents

DILUTION

If you invest in our common stock, your ownership interest will be diluted by the amount by which the initial offering price per share paid by the purchasers of common stock in this offering exceeds the net tangible book value per share of our common stock following this offering. As of March 31, 2007, our net tangible book value was approximately $(3.9) million, or $ per share of common stock. Net tangible book value per share equals total tangible assets minus total liabilities and the series A convertible preferred stock divided by the number of shares of our common stock outstanding.

Our pro forma net tangible book value as of March 31, 2007 would have been approximately $ million, or $ per share of common stock, after giving effect to:

- the sale by us of common stock in this offering, based on an assumed initial public offering price of $ per share (the midpoint of the range shown on the cover page of this prospectus) and after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us;
- the repayment of all amounts outstanding under our senior secured loan agreement (approximately $7.9 million as of March 31, 2007);
- the conversion of 7,952,018 shares of series A convertible preferred stock held by TA Associates that were outstanding prior to this offering into shares of common stock;
- the expected satisfaction of the stock compensation liability associated with the variable performance equity agreement between Tom Sullivan and Kevin Sullivan, which includes a guarantee by us, through the transfer of shares of common stock from Tom to Kevin; and
- the non-cash compensation expense associated with the regional manager stock unit plan and acceleration of non-cash compensation expense under the 2004 and 2006 stock option plans.

This represents an immediate increase in the net tangible book value of $ per share to existing stockholders and an immediate dilution in the net tangible book value of $ per share to the investors who purchase our common stock in this offering at the initial offering price. Sales of shares by our selling stockholders in this offering do not affect our net tangible book value. The following table illustrates this per-share dilution:

Initial public offering price per share	
Net tangible book value per share as of March 31, 2007	
Increase in net tangible book value per share attributable to this offering	
Decrease in net tangible book value per share attributable to conversion of the series A convertible preferred stock	
Pro forma net tangible book value per share after this offering	
Dilution per share to new investors in this offering	

Table of Contents

The following table summarizes, on a pro forma basis, as of March 31, 2007, the difference between existing stockholders and new investors with respect to the number of shares of common stock purchased from us, the total consideration paid to us for these shares and the average price per share paid by our existing stockholders and to be paid by the new investors in this offering. The calculation below reflecting the effect of shares purchased by new investors is based on an initial public offering price of $ per share (the midpoint of the range shown on the cover page of this prospectus), before deducting underwriting discounts and commissions and estimated offering expenses payable by us.

	Shares Purchased		Total Consideration		Average Price
	Number	Percent	Amount	Percent	Per Share
Existing stockholders					
New investors					
Total					

The share information in the tables above excludes:

- shares of common stock issuable upon exercise of outstanding stock options with a weighted average exercise price of $ per share, of which were vested as of , 2007;
- restricted stock grants of shares of common stock that we intend to grant to certain executive officers and employees at the closing of the initial public offering; and
- stock option grants that we intend to grant certain directors on the day this offering is priced for sale to the public to purchase shares of common stock at the initial public offering price.

If outstanding options are exercised, new investors will experience further dilution.

Table of Contents

UNAUDITED PRO FORMA FINANCIAL INFORMATION

The unaudited pro forma balance sheet as of March 31, 2007 gives pro forma effect to the following transactions as if they each occurred on March 31, 2007 and the unaudited pro forma income statement for the year ended December 31, 2006 and for the three months ended March 31, 2007 gives pro forma effect to the following transactions as if they occurred on January 1, 2006:

- the sale by us of common stock in this offering, based on an assumed initial public offering price of $ per share (the midpoint of the range shown on the cover page of this prospectus) and after deducting the underwriting discounts and commissions and estimated offering expenses payable by us;
- the repayment of all amounts outstanding under our senior secured loan agreement;
- the conversion of 7,952,018 shares of series A convertible preferred stock held by TA Associates that were outstanding prior to this offering into shares of common stock;
- the grant of shares of restricted common stock to certain executive officers and employees, reflecting shares that we intend to grant to such persons at the closing of the initial public offering;
- stock option grants that we intend to grant certain directors on the day this offering is priced for sale to the public to purchase shares of common stock at the initial public offering price;
- the expected satisfaction of the stock compensation liability associated with the variable performance equity agreement between Tom Sullivan and Kevin Sullivan, which includes a guarantee by us, through the transfer of shares of common stock from Tom to Kevin; and
- the non-cash compensation expense associated with the regional manager stock unit plan and acceleration of non-cash compensation expense under the 2004 and 2006 stock option plans.

The unaudited pro forma financial information is presented for informational purposes only and does not purport to represent what our results of operations would actually have been if the transactions had occurred on the dates indicated nor do they purport to project our results of operations for any future period.

You should read our unaudited pro forma financial statements and the accompanying notes in conjunction with all of the historical financial statements and related notes included in this prospectus and other financial information appearing elsewhere in this prospectus, including information contained in Capitalization and Management s Discussion and Analysis of Financial Condition and Results of Operations.

Lumber Liquidators, Inc.

Unaudited Pro Forma Balance Sheet

(in thousands)

	As of March 31, 2007		
	Actual	**Offering Adjustments**	**Pro Forma**
Assets			
Current assets:			
Cash and cash equivalents	$ 5,145		
Merchandise inventories	63,472		
Prepaid expenses	4,080		
Other current assets	2,408		
Total current assets	75,105		
Property and equipment, net	9,307		
Deferred income taxes	4,075		
Other assets	2,507		
Total assets	$ 90,994		
Liabilities and Stockholders Equity (Deficit)			
Current liabilities:			
Accounts payable	$ 20,819		
Customer deposits and store credits	9,566		
Stock compensation liability	9,534		
Accrued compensation	2,342		
Other current liabilities	8,455		
Current portion of long-term debt	2,076		
Current portion of capital lease obligations	206		
Total current liabilities	52,998		
Long-term debt	5,972		
Capital lease obligations	30		
Redeemable preferred stock	34,808		
Stockholders equity (deficit)	(2,814)		
Total liabilities and stockholders equity (deficit)	$ 90,994		

See accompanying notes to unaudited pro forma balance sheet

Table of Contents

Notes to Unaudited Pro Forma Balance Sheet

Set forth below are the estimated sources and uses of funds pertaining to this offering.

Sources	(in thousands)
Proceeds from offering of common stock, net of estimated fees and expenses	
Total sources	
Uses	
Repayment of all amounts outstanding under our senior secured loan agreement (approximately $7.9 million as of March 31, 2007)	
Cash available for general corporate purposes	
Total uses	

This offering is expected to raise proceeds of $ million (net of estimated fees and expenses, and based on the midpoint of the range shown on the cover page of this prospectus) to us. Had the offering occurred on March 31, 2007, it would have had the following effect on our balance sheet:

Cash and cash equivalents would have increased by the cash available for general corporate purposes.

Debt would have decreased as the proceeds would have been used to repay $7.9 million under our senior secured loan agreement.

Stock compensation liability of $9.5 million associated with the variable performance equity agreement would be converted to stockholders equity with the expected transfer of shares of common stock from Tom Sullivan to Kevin Sullivan.

The liability related to the series A convertible preferred stock would become stockholders equity upon conversion to shares of common stock.

The increase in stockholders equity of $ million would have been attributable to $ million in proceeds needed to repay our senior secured loan agreement and $ as a result of tax benefits associated with stock-based compensation.

Table of Contents

Lumber Liquidators, Inc.

Unaudited Pro Forma Statement of Income

(in thousands)

	Year Ended December 31, 2006			Three Months Ended March 31, 2007		
	Actual	**Offering Adjustments(1)**	**Pro Forma**	**Actual**	**Offering Adjustments(1)**	**Pro Forma**
Net sales	$ 332,060			$ 92,022		
Cost of sales	221,931			61,451		
Gross profit	110,129			30,571		
Selling, general and administrative expenses	88,716			26,816		
Operating income	21,413			3,755		
Interest expense	722			174		
Other (income) expense(2)	(368)			(55)		
Income before income taxes	21,059			3,636		
Provision for income taxes	8,161			1,405		
Net income	$ 12,898			$ 2,231		
Net income per common share(3):						
Basic	$ 0.86			$ 0.15		
Diluted	$ 0.56			$ 0.10		
Weighted average common shares outstanding:						
Basic	15,000,100			15,000,100		
Diluted	22,989,403			22,952,118		

See accompanying notes to unaudited pro forma statement of income

Table of Contents

Notes to Unaudited Pro Forma Statement of Income

(1) Reflects the following adjustments:

(a) Elimination of interest expense incurred since January 1, 2006 from our borrowings under the senior secured loan agreement.

(b) Application of the appropriate statutory tax rates of the respective tax jurisdictions to which adjustments relate, 38.8% in 2006.

(c) Adjustment of the stock compensation expense in 2006 associated with the variable performance equity agreement between Tom Sullivan and Kevin Sullivan, which includes a guarantee by us.

(d) Increased stock compensation expense related to the acceleration of certain stock option agreements and the triggering event for the Regional Manager Stock Unit Plan.

(e) Restricted stock grants of shares of common stock that we intend to grant to certain executive officers and employees at the closing of the initial public offering.

(f) Stock option grants that we intend to grant certain directors on the day this offering is priced for sale to the public to purchase shares of common stock at the initial public offering price.

A $1 change, up or down, in the midpoint of the range shown on the cover page of this prospectus would change the stock compensation liability expense associated with the agreement between Tom Sullivan and Kevin Sullivan by $ and the non-cash compensation expense associated with the regional manager stock unit plan by $.

(2) Includes interest income.

(3) Pro forma basic and diluted net income per common share are computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period and include the effect of issuing additional shares of common stock at a price of $ per share in this offering.

The following table summarizes the pro forma effect to our earnings per share (EPS):

	Year Ended December 31, 2006	Three Months Ended March 31, 2007
Pro forma (unaudited) weighted average common shares outstanding, including preferred stock conversion to common stock		
Effect of shares issued		

Pro forma weighted average common shares outstanding including effect of shares issued	
Dilutive effect of stock options	
Pro forma weighted average common shares and dilutive securities outstanding	

29

Table of Contents

SELECTED FINANCIAL DATA

You should read the data set forth below in conjunction with our financial statements and related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations, Unaudited Pro Forma Financial Information and other financial information included elsewhere in this prospectus. We derived the selected financial data as of December 31, 2005 and 2006 and for each of the years ended December 31, 2004, 2005 and 2006 from our audited financial statements and the related notes appearing elsewhere in this prospectus. We derived the selected financial data as of December 31, 2004 from our audited financial statements and the related notes not included in this prospectus. We derived the selected financial data as of and for the years ended December 31, 2002 and 2003 from our unaudited financial statements not included in this prospectus. The selected statements of income data for the three months ended March 31, 2006 and 2007 and the selected balance sheet data as of March 31, 2007 have been derived from our unaudited financial statements appearing elsewhere in this prospectus which, in the opinion of our management, have been prepared on the same basis as the audited financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of our operating results and financial position for those periods and as of those dates. The selected unaudited financial data for the three months ended March 31, 2007 are not necessarily indicative of our results for the year ending December 31, 2007 and our historical results are not necessarily indicative of our results for any future period.

	Year Ended December 31,					Three Months Ended March 31,	
	2002	2003	2004	2005	2006(1)	2006(1)	2007(1)
	(in thousands, except share and per share amounts)						
	(unaudited)	(unaudited)				(unaudited)	(unaudited)
Statement of Income Data							
Net sales	$ 65,382	$ 100,866	$ 171,766	$ 244,947	$ 332,060	$ 76,051	$ 92,022
Cost of sales	43,051	67,870	115,857	158,844	221,931	49,642	61,451
Gross profit	22,331	32,996	55,909	86,103	110,129	26,409	30,571
Selling, general and administrative expenses	17,545	29,566	48,461	67,900	88,716	20,537	26,816
Impairment loss on long-lived assets		955	293				
Operating income	4,786	2,475	7,155	18,203	21,413	5,872	3,755
Interest expense	160	218	429	638	722	167	174
Other (income) expense(2)	(318)	(428)	190	(96)	(368)	(107)	(55)
Income before income taxes	4,944	2,685	6,536	17,661	21,059	5,812	3,636
Provision for income taxes(3)	163	65	(1,450)	6,948	8,161	2,252	1,405
Net income	$ 4,781	$ 2,620	$ 7,986	$ 10,713	$ 12,898	$ 3,560	$ 2,231
Net income per common share:							
Basic	$ 0.32	$ 0.17	$ 0.53	$ 0.71	$ 0.86	$ 0.24	$ 0.15
Diluted	$ 0.32	$ 0.17	$ 0.51	$ 0.46	$ 0.56	$ 0.15	$ 0.10
Weighted average common shares outstanding(4):							
Basic	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100

Diluted	15,000,100	15,000,100	15,675,477	23,063,174	22,989,403	23,037,415	22,952,118

(1) We adopted the provisions of SFAS 123 (R), using the prospective-transition method, effective January 1, 2006.
(2) Includes interest income.

Table of Contents

(3) Effective December 1, 2004, we elected to be taxed as a C corporation for federal and state income tax purposes. Prior to this election, we were not subject to federal and certain state income taxation at the corporation level.

(4) Share amounts as of December 31, 2002 and 2003 have been adjusted to reflect the December 2004 common stock dividend of 150,000:1 to Tom Sullivan, our founder and chairman of our board of directors.

	As of December 31,					As of March 31,
	2002	2003	2004	2005	2006	2007
			(in thousands)			
	(unaudited)	(unaudited)				(unaudited)
Balance Sheet Data						
Cash and cash equivalents	$ 384	$ 3,073	$ 3,031	$ 6,031	$ 3,965	$ 5,145
Merchandise inventories	9,501	14,910	22,507	30,009	51,758	63,472
Total assets	13,249	21,017	39,753	55,162	78,020	75,105
Total debt and capital lease obligations, including current maturities	2,555	2,617	12,364	10,360	9,603	8,284
Stock compensation liability	850	2,020	4,958	8,092	9,132	9,534
Redeemable preferred stock			34,693	34,744	34,795	34,808
Total stockholder s equity (deficit)	4,260	3,620	(30,242)	(18,775)	(5,468)	(2,814)
Working capital(1)	4,299	5,230	8,091	17,059	29,697	22,107

(1) Working capital is defined as current assets minus current liabilities.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion together with Selected Financial Data and our financial statements and related notes included elsewhere in this prospectus. The discussion contains forward-looking statements involving risks, uncertainties and assumptions that could cause our results to differ materially from expectations. Factors that might cause these differences include those described under Risk Factors, Forward-Looking Statements and elsewhere in this prospectus.

Overview

Lumber Liquidators is the largest specialty retailer of hardwood flooring in the United States, based on total sales. We offer an extensive selection of premium hardwood flooring products from more than 25 domestic and exotic wood species under multiple proprietary brands, together with a broad assortment of flooring enhancements and installation accessories, at everyday low prices that appeal to a diverse customer base. We purchase flooring directly from supplier mills and brokers, thereby avoiding mark-ups by distributors. As of May 31, 2007, we sold our products through 98 Lumber Liquidators stores in 40 states, a call center, our website and a catalog. Our low-cost store model utilizes a no frills showroom with limited in-store inventory. We currently finish 75% of our premium Bellawood products at our Toano finishing line and distribution center to ensure product quality and to reduce third-party finishing costs. Approximately 85% of our merchandise passes through this facility before we move it to our stores. We believe that our vertically integrated business model enables us to offer a broad assortment of high-quality products to our customers at a lower cost than our competitors.

The growth in our net sales has been driven by new store openings and our strong comparable store sales performance. In the period from January 1, 2003 to May 31, 2007, we opened 74 stores, 69 of which were open as of March 31, 2007, representing more than two-thirds of our total store base. Our gross profit is driven primarily by the cost of acquiring the products we sell from our suppliers, but also includes inbound transportation costs from those suppliers to our distribution center or stores, customs and duty charges, transportation charges from our distribution center to our stores and the cost of delivering product purchases to the customer. Our most significant operating expenses have historically been our advertising expenses and our labor costs. Our advertising costs have generally declined as a percentage of net sales as we have expanded, but may vary from quarter to quarter with shifts in marketing strategy and the timing of our marketing campaigns. Our labor costs have also declined as a percentage of net sales, while increasing in absolute terms as a result of our investment in the store support infrastructure, including enhancements to our management team. We expect that our aggregate operating expenses will decline as a percentage of our net sales as we implement our growth strategy and our business continues to grow.

In late 2005, we began a two-year program to implement various initiatives to improve our infrastructure and to position our business to support sustainable growth and profitability in the future. These initiatives included:

Investing in our infrastructure. In response to the rapid growth in the number of new store locations that began in 2003, we slowed the pace of new store openings in 2006 to focus on expanding our store support infrastructure. As part of this process, we have assembled an experienced executive team to manage our day-to-day operations and reinforce the foundation that will enable us to achieve our long-term growth objectives. In September 2006, we hired our chief executive officer, and our founder transitioned to become the chairman of our board of directors, where he remains actively involved developing and executing our marketing strategy, and enhancing the relationships with our supplier mills and brokers. During 2006 and 2007, we also hired several individuals with significant experience in the specialty retail industry, including a new chief information officer, a new senior vice president of store operations and a senior vice president of merchandising. We have also expanded our management structure by adding senior vice presidents of direct marketing and advertising and e-commerce and a general counsel. We have also restructured our regional operations by increasing the number of regional managers from eight to 14 to support future growth and assist in maintaining pricing and cost discipline.

Expanding product assortment and improving our ability to meet customer requirements. We have expanded our product offerings to include a broader assortment of key product lines, including engineered hardwoods and solid hardwoods by Dura-Wood. We believe that presenting customers with a broader assortment of products with narrower price point differentials encourages customers to trade up to our premium products. We have also increased our emphasis on moldings and accessories, which enable us to make valuable add-on sales. In addition, we refined our merchandising strategy to optimize inventory levels through purchasing and logistics efforts to best match product availability with customers varying delivery needs.

Although the hardwood flooring market is projected to experience long-term growth, estimated at a compound annual growth rate of 7.4% through 2011, Catalina Research Inc. estimates that U.S. hardwood flooring sales declined by 10.6% in 2006, with a 15.2% decline in square-foot sales in the fourth quarter of 2006. Similar declines were estimated across most types of flooring, and were due in particular to decreased new housing demand. Despite these market declines, however, our net sales increased 36% in 2006. See Business Our Market. Although the majority of our sales are to consumers engaged in remodeling projects, a decline in new housing demand could cause a decline in remodeling or remodeling activity could decline for other reasons. See Risk Factors Risks Relating to Our Business and Industry The hardwood flooring industry depends on the economy, home remodeling activity, the homebuilding industry and other important factors. We believe that we will continue to benefit from several key long-term industry trends and characteristics, including increased home improvement spending resulting from aging housing stock, increasing home ownership, increasing average home size and favorable demographic trends as well as the expansion and evolution of the hardwood flooring market and the greater perceived attractiveness of hardwood flooring among consumers.

Assessing the Performance of Our Business

In assessing the performance of our business, we consider a variety of performance and financial measures. The key measures we use to determine how our business is performing are net sales and comparable store sales. Some of the operational metrics that we consider in evaluating net sales include our sales mix, future demand as measured by open orders and the related customer deposits, the average number of days an order/customer deposit is outstanding, requests for samples and catalogs, new store performance levels and our new store pipeline. In assessing the overall performance of our business, we also consider gross profit and selling, general and administrative expenses.

Net Sales

We derive net sales primarily from sales of solid and engineered hardwood, laminate, bamboo and cork flooring products, moldings and flooring accessories made through our stores, call center, website and catalog. Net sales include freight costs billed to customers and are net of any returns by customers. Net sales from customer orders placed through the call center, our website or our catalog are recorded by the store where the customer picks up the merchandise or schedules delivery. Several factors affect our net sales in any period, including the number of stores in operation and comparable store sales for any given store or group of stores, which can be influenced by our operational effectiveness, pricing, marketing and promotional efforts, brand recognition levels, local competition and trade area demographics.

Growth In Our Store Base. We opened 17 stores in 2004, 19 stores in 2005 and 16 stores in 2006, which contributed substantially to the growth of our net sales in those years. In 2006, we slowed the increase in new store locations as we expanded our store support infrastructure to better facilitate sustainable growth of both our net sales and gross margin. As of May 31, 2007, we had opened seven new stores (two in the first quarter) and had signed leases for eight additional stores during 2007. We plan to open at least 25 new stores in 2007 and between 30 and 40 new stores during each of the next several years thereafter. The cost required to open a typical new store is approximately $240,000, of which inventory, net of trade payables, represents approximately $190,000. Our new stores have historically opened with an initial ramp-up period typically lasting from 36 to 48 months or more, during which they generated sales below the levels at which we expect them to normalize. Our average new store across our markets has, however, historically become profitable within three months of beginning operations and returned its initial cash investment within seven months. See Risk Factors Risks Related to Our Business and Industry The planned rapid increase in the number of our stores may make our future results unpredictable.

Comparable Store Sales. The other important driver of growth in our net sales has been increased comparable store sales, which accounted for a substantial portion of our historical net sales growth. Stores enter the comparable store base on the first day of the thirteenth full calendar month after they open. Various factors affect comparable store sales, including:

- consumer preferences, buying trends and overall economic trends and our ability to anticipate and respond effectively to changes therein;
- changes in our overall merchandise sales mix and changes in our sales mix with respect to each of our sales channels;
- pricing;
- the timing of our promotional events;
- competition;
- our ability to source and distribute products efficiently;
- the number of stores we open or close in any period; and
- weather and other climatological effects.

We believe that future comparable store sales will likely increase at rates slower than those achieved over the past several years, due to increases in baseline store volumes and an increase in the number of new stores opened in existing markets, which tend to open at a higher base level of sales. See Risk Factors Risks Related to Our Business and Industry Failure to manage our growth effectively could harm our business and operating results.

Gross Profit and Gross Margin

Gross profit is equal to our net sales minus our cost of sales, and gross margin is equal to gross profit as a percentage of net sales. Our gross profit has historically been affected by, among other things:

our sales volumes and the margins on products we sell;

the mix of our products sold and the related cost of that merchandise, including in particular the cost of hardwood and other flooring products and accessories;

transportation costs, both from our suppliers to our distribution center or stores and from our distribution center to our stores, which may vary with factors such as fuel costs;

customs and duty charges on international purchases;

- the cost of third-party carrier services providing customer deliveries;
- in-house finishing costs, particularly for our Bellawood brand;
- the costs of providing samples requested by our customers;
- inventory adjustments, including shrinkage;
- the extent of any mark-downs and the volume of inventory impacted by sales and promotional events; and
- competition.

We try to minimize the volatility of hardwood prices which represents the largest portion of our cost of sales by relying on our close relationships with our suppliers and utilizing our financial flexibility to establish beneficial payment terms. Generally, we strive to match merchandise purchase lead times with anticipated demand to maximize sustainable gross margins, and those lead times currently range by product from approximately 90 to 180 days.

We work to improve gross profits and gross margin on an ongoing basis through inventory management improvements, logistics alternatives, pricing levels, promotional activities and vendor relationships, among other things. Several of our recent initiatives to position our business for more effective future growth have also had a significant impact on our gross margins, and we continue to assess various opportunities. We continually review our inventory levels and sales mix on a regular basis to identify slow-moving merchandise and products which do not meet our quality standards and cannot be sold at full price, and generally use promotional events and mark-downs to clear that inventory. We believe that, taken together, the changes we have made and intend to implement should enable us to sustain and gradually increase our gross margins in future periods. Our gross profits and gross margins may not be comparable to other companies that record different costs as components of cost of sales.

Selling, General, Administrative and Other Operating Expenses

Advertising Expenses. The largest component of our selling, general and administrative (SG&A) expenses is advertising expenses at the national, regional and local level, as well as costs associated with publishing our catalogs and maintaining our website. We have made a significant investment in advertising to develop our national brands, including our portfolio of proprietary product offerings. We believe Lumber Liquidators is now recognized across the United States as a destination for high-quality hardwood flooring at everyday low prices. We have historically focused on national advertising, including buying ads in national publications, using targeted television advertising, co-sponsoring television shows, advertising on syndicated radio programs and sports marketing. In the future, we expect to place greater focus on local advertising to support targeted store growth and in connection with new store openings while maintaining appropriate levels of national advertising. As we open more stores we expect to see greater returns on our investment in national advertising as more stores open near potential customers who have already been introduced to our brands. In addition, while our advertising costs may vary from quarter to quarter with shifts in marketing strategy and the timing of our marketing campaigns, we believe that the percentage of our net sales devoted to marketing and advertising will generally decline as we continue to grow. See Risk Factors Risks Relating to Our Business and Industry Our success depends on the continued effectiveness of our advertising strategy.

Labor Costs. The second-largest component of our SG&A expenses is expenses relating to employees, consisting principally of salaries, commissions and benefits paid to employees in our stores which increase as we open more stores and employees in our distribution facility and headquarters which should increase more slowly as we grow. Most of our labor costs relate to staff at our stores and our distribution facility. However, labor costs have recently increased significantly as we improved our store support strategies and operational infrastructure, positioning our business for more effective and sustainable future growth. We believe that the percentage of our net sales devoted to labor costs will generally decline as we continue to grow.

Other Expenses. Our SG&A expenses also include occupancy costs for our stores, warehouse and headquarters (including rent, utilities, real estate taxes and maintenance charges); costs relating to our delivery fleet (including payroll and maintenance); equity compensation expenses; credit and debit card discount and processing fees; depreciation and amortization; bank fees; legal and professional fees; and other corporate and administrative functions that support our stores. SG&A expenses also include store opening costs, which we expense as they are incurred. In 2004, our operating expenses also included an impairment loss on long-lived assets relating to the relocation of our finishing line and corporate headquarters to Toano.

Other Factors Affecting Our Results

Equity Compensation Expenses

We maintain three equity compensation plans: a stock option plan for executive management; a stock option plan for non-employee members of our board of directors; and a stock unit plan for regional store management. We have not recorded any compensation expense relating to the stock unit plan because those options would have expired without value unless an IPO or sale event occurs before 2011. In addition, we intend to make restricted stock grants to certain executive officers and employees at the closing of the initial public offering. In connection with this offering, we expect to incur a charge of approximately $ million (based on the midpoint of the range shown on the cover page of this prospectus) in the quarter of 2007 in which this transaction closes relating to the stock unit plan, the restricted stock grant and acceleration of options under the 2004 and 2006 stock option plans.

We are also party to a stock-based agreement between Tom Sullivan and Kevin Sullivan, Tom s brother, who started our western U.S. operations and was our first regional manager, pursuant to which we generally guarantee Tom s cash payment obligation under the agreement. We account for that agreement as a variable performance plan. Under that agreement, as amended in August 2005, Kevin has the right to a fixed ownership percentage of Lumber Liquidators, Inc. on a fully diluted basis, plus an additional ownership percentage based on certain performance criteria. This right is exercisable for shares of common stock, to be contributed by Tom and which have been placed in escrow, in conjunction with an IPO or sales event. Kevin s right under the plan will be considered to be exercised in full immediately prior to the completion of the initial public offering and, accordingly, we do not expect to record any future charges relating to this plan other than a charge in connection with the IPO of $ (based on the midpoint of the range shown on the cover page of this prospectus) in the quarter of 2007 in which this transaction closes. Before the agreement was amended in August 2005, we recorded stock-based compensation expense based on Kevin having earned a 5% ownership interest on a fully diluted basis (in conformity with the terms of that agreement). We recorded stock-based compensation expense relating to the agreement of $0.4 million in the first quarter of 2007, $1.0 million in 2006, $3.1 million in 2005 and $2.9 million in 2004, and carried a short-term liability on our balance sheet relating to the agreement of $9.5 million at March 31, 2007. See Risk Factors Risks Relating to Our Business and Industry We will incur non-cash compensation expenses, and may be required to issue shares of common stock, in connection with existing stock-based compensation agreements. A $1 change, up or down, between the price set forth above and the price of stock on the trading day before the closing of this offering would change the non-cash compensation expense associated with the agreement between Tom Sullivan and Kevin Sullivan by $.

In addition, we had an employment agreement and a stock warrant plan with a former senior executive (who resigned on May 31, 2006). The former executive alleges that he terminated his

Table of Contents

employment for good reason, as defined in his employment agreement and the warrant plan. Under the provisions of his employment agreement, his termination for good reason could entitle him to up to two years of wages and benefits, while under the provisions of the warrant plan, he could be entitled to shares in an amount equal to up to 1.0% of our outstanding common stock. Stock-based compensation expenses under this plan for 2005 and 2004 were reversed in 2006 upon separation, with an offset to additional capital. See Business Litigation.

For additional information regarding our equity compensation plans, see Management Executive Compensation and Note 7 to our financial statements.

Income Taxes

Effective December 1, 2004, we elected to be taxed as a C corporation for federal and state income tax purposes, and we have provided for income taxes since that date. The effect of initially recognizing deferred tax assets and liabilities related to this change in tax status was included in the provision for income taxes for 2004. We were not subject to federal and certain state income taxation at the corporation level prior to that election. Our effective tax rate will vary based on state-tax allocations and future tax minimization strategies in future periods.

Results of Operations

The following tables set forth components of our results of operations for the periods indicated, both in dollars and as a percentage of net sales.

	Year Ended December 31,			Three Months Ended March 31,	
	2004	2005	2006	2006	2007
			(in millions)		
Net sales	$ 171.8	$ 244.9	$ 332.1	$ 76.1	$ 92.0
Comparable sales increase from prior year	*38.2%*	*19.0%*	*17.3%*	*24.1%*	*8.5%*
Number of stores opened in period	*17*	*19*	*16*	*4*	*2*
Cost of sales	115.9	158.8	221.9	49.6	61.5
Gross profit	55.9	86.1	110.1	26.4	30.6
SG&A expenses	48.5	67.9	88.7	20.5	26.8
Operating income	7.2	18.2	21.4	5.9	3.8
Net income(1)	8.0	10.7	12.9	3.6	2.2

	Year Ended December 31,			Three Months Ended March 31,	
	2004	2005	2006	2006	2007
			(% of net sales)		
Net sales	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of sales	67.5%	64.8%	66.8%	65.3%	66.8%
Gross profit	32.5%	35.2%	33.2%	34.7%	33.2%
SG&A expenses	28.2%	27.7%	26.7%	27.0%	29.1%
Operating income	4.2%	7.4%	6.4%	7.7%	4.1%
Net income(1)	4.6%	4.4%	3.9%	4.7%	2.4%

(1) Effective December 1, 2004, we elected to be taxed as a C corporation for federal and state income tax purposes. Prior to this election, we were not subject to federal and certain state income taxation at the corporation level.

Table of Contents

Three Months Ended March 31, 2007 Compared to Three Months Ended March 31, 2006

Net Sales. Net sales increased approximately $16.0 million, or 21.0%, to $92.0 million in the first quarter of 2007 from $76.1 million in the first quarter of 2006. This increase was primarily driven by an increase of $6.4 million, or 8.5%, in comparable store sales, and by a $9.6 million increase in non-comparable net sales at the 14 stores opened during the twelve-month period ended March 31, 2007, partially offset by the closing of one store in May 2006. Comparable store sales increases were driven primarily by the continued maturation of stores in operation for 13 to 36 months, where net sales increased $4.8 million, or 20.9%, and generally strong consumer demand for our expanded product assortment. Overall, our net sales volume, primarily measured in square footage, increased 22.2% due to store maturation, offsetting a slight decline in the average retail price per unit sold. We opened more new store locations in existing markets in the twelve months ended March 31, 2007 than we had in the twelve months ended March 31, 2006, and although these multiple-store markets have increased total sales, they typically dampen comparable store sales increases until all stores in the market are considered comparable.

Gross Profit and Gross Margin. Gross profit increased approximately $4.2 million, or 15.8%, to $30.6 million in the first quarter of 2007 from $26.4 million in the first quarter in 2006, principally due to increases in net sales that were partially offset by higher costs from suppliers for the merchandise sold and an increase in transportation costs.

Gross margin in the first quarter of 2007 was 33.2%, decreasing from 34.7% in the first quarter of 2006, but comparable to the overall gross margin for 2006. In the first quarter of 2006, we began an initiative to broaden both our assortment of products and the retail price points available to our customers. The new products that we introduced, primarily the prefinished engineered hardwoods, drove increases in net sales and gross profit but have a gross margin lower than our average product. Engineered hardwoods represented 11.4% of net sales in the first quarter of 2007 as compared to 6.1% in the first quarter of 2006. Higher domestic and international transportation costs also caused gross margin to decline, as per-mile ground charges increased, primarily due to higher fuel costs.

Operating Income. Operating income for the three months ended March 31, 2007 decreased $2.1 million, or 36%, to $3.8 million for the three months ended March 31, 2007, as a $4.2 million increase in gross profit was more than offset by a $6.3 million increase in SG&A expenses, principally due to the following factors:

- Advertising expenses increased $1.9 million, or 22.1%, to $10.5 million in the first quarter of 2007 primarily due to the expansion of both our national advertising branding campaign through television, radio and sports marketing, and our direct mail programs. As a percentage of net sales, advertising expenses increased to 11.4% of net sales for the three months ended March 31, 2007 from 11.3% of net sales for the three months ended March 31, 2006 as the timing of direct mail programs caused us to recognize more advertising expenses in the first quarter of 2007. This increase was partially offset by our ability to further leverage our national advertising over increased net sales across all our sales channels.

- Salaries, commissions and benefits increased $2.4 million, or 37%, in the first quarter of 2007 primarily due to both the increase in the number of new store locations and the significant investment in executive and operational management within our store support infrastructure. The investment in executive and operational store support management after March 31, 2006 included our new chief executive officer, four senior executive positions that did not exist prior to March 31, 2006, an increase in the number of regional store managers and enhanced financial and information technology control and compliance positions. Accordingly, as a percentage of net sales, salaries, commissions and benefits increased to 9.7% in the first quarter of 2007 from 8.6% in the first quarter of 2006.

Table of Contents

Stock-based compensation expense increased to $0.8 million in the first quarter of 2007 from $0.3 million in the first quarter of 2006 due to options granted in July and October 2006, and an increase in the stock compensation calculated under Kevin s agreement with Tom.

Occupancy costs increased to $2.7 million in the first quarter of 2007 from $2.4 million in the first quarter of 2006 principally due to the 14 stores opened during the twelve-month period ended March 31, 2007, but declined to 3.0% of net sales from 3.2% in the first quarter of 2006, as increases due to those store openings was more than offset by our ability to leverage costs relative to our Toano facility over increased net sales.

As a percentage of net sales, operating income declined to 4.1% for the three months ended March 31, 2007 from 7.7% for the three months ended March 31, 2006. This decrease was primarily due to the decline in gross margin and an increase in SG&A expenses as a percentage of net sales to 29.1% for the quarter ended March 31, 2007 from 27.0% for the quarter ended March 31, 2006.

Net Income. Net income decreased approximately $1.4 million to $2.2 million for the three months ended March 31, 2007 from $3.6 million for the three months ended March 31, 2006 and declined as a percentage of net sales to 2.4% in the first quarter of 2007 from 4.7% in the first quarter of 2006. Our effective income tax rate was approximately 38.7% for the first quarter of 2007 compared to 38.8% for the first quarter of 2006, reflecting slight variances in state income tax rates.

Year Ended December 31, 2006 Compared to Year Ended December 31, 2005

Net Sales. Net sales increased $87.1 million, or 36%, to $332.1 million in 2006 from $244.9 million in 2005. This increase was primarily driven by an increase of $42.0 million, or 17.3%, in comparable store sales, and by a $28.7 million increase in non-comparable net sales at the 19 stores opened during 2005, and $16.4 million at the 16 new stores opened during 2006. Comparable store sales increases were driven principally by maturation of new stores, optimization of our product mix to reflect customer demand and increased traffic across our store base. The average retail price per unit sold also increased slightly. Overall net sales increased due principally to the following factors:

In early 2006, we introduced a number of new prefinished engineered hardwood products over a range of retail price points not previously available, which increased sales in those product categories. We also continued to increase the percentage of our net sales represented by moldings and accessories, from 7% in 2005 to 8% in 2006.

Increases in comparable store sales and non-comparable net sales also resulted from the continuing maturation of our store base, as net sales at stores open for less than 36 months (56% of our stores in operation as of December 31, 2006) increased faster than our more mature stores.

Net sales also increased due to improvements we made to our website that, among other things, made it easier to place orders over the Internet.

Gross Profit and Gross Margin. Gross profit increased $24.0 million, or 28%, to $110.1 million in 2006 from $86.1 million in 2005, principally as a result of increases in net sales that were partially offset by higher average supplier costs and an increase in transportation costs. Gross margin decreased approximately 200 basis points to 33.2% in 2006 from 35.2% in 2005, which was principally due to the following factors:

The implementation of our 2006 initiative to broaden our product range increased net sales but caused our gross margin to decline. In particular, we expanded our sales mix to include some products, such as engineered hardwoods, that have a lower gross margin than our average product, which caused an approximately 120 basis point decline in gross margin. The introduction of additional products in our Dura-Wood line also caused an approximately 30 basis

Table of Contents

point decline in gross margin, as those products have a lower gross margin than our average product and because we implemented a retail pricing strategy designed to enable those products to gain market share.

As part of our efforts to optimize inventory levels, we implemented a number of price discounts (primarily during the fourth quarter of 2006) with respect to slower-moving inventory. We also were required to increase reserves for product warranties due to a purchase of defective merchandise from one supplier. These actions collectively resulted in an approximately 30 basis point decline in our gross margin.

Decreases in the prices of certain product categories, particularly laminates and bamboo, designed to increase net sales and optimize our product mix, which were further impacted by supplier unit cost increases that were not passed on proportionately to our customers, resulted in an approximately 25 basis point decline in gross margin.

Higher domestic and international transportation costs, primarily due to higher fuel and ocean freight costs, customs duties and per-mile ground charges, also caused a decline in gross margin.

These decreases were partially offset by increases in gross margin that resulted from increased efficiencies at our Toano finishing line, slightly higher sales volumes of moldings and accessories (as those products generally have a higher gross margin than that our average product) and savings from new, longer-term international transportation contracts.

Operating Income. Operating income increased $3.2 million, or 18%, to $21.4 million in 2006, principally as a result of the $24.0 million increase in gross profit that was partially offset by a $20.8 million increase in SG&A expenses principally due to the following factors:

Advertising expenses increased $8.7 million, or 32%, in 2006 primarily due to the expansion of our national advertising campaign through television, radio and sports, as well as increased costs relating to online advertising and direct mail programs. As a percentage of net sales, advertising expenses declined to 10.9% in 2006 from 11.3% in 2005, principally due to our ability to leverage our national advertising over increased net sales across all our sales channels.

Salaries, commissions and benefits increased $6.1 million, or 26%, in 2006 primarily due to an increase in the store support infrastructure principally in the second half of 2006, including the hiring of our new chief executive officer and other executives and operational managers. As a percentage of net sales, salaries, commissions and benefits paid to our employees declined to 8.9% in 2006 from 9.6% in 2005, principally due to our ability to leverage our store support infrastructure over increased net sales, although several of the additional costs were not recognized over the full year.

Occupancy costs increased $2.3 million, or 28%, in 2006 principally due to 16 new stores opened in 2006 and the full-year impact of 19 stores opened in 2005. As a percentage of net sales, occupancy costs decreased to 3.1% in 2006 from 3.3% in 2005.

Professional expenses increased $0.8 million to support enhanced financial reporting, legal and regulatory compliance, internal controls and corporate governance functions.

Stock-based compensation expense decreased due to lower current-year expense associated with Kevin s agreement with Tom, which was partially offset by expense related to stock options granted in 2006.

As a percentage of net sales, operating income declined to 6.4% in 2006 from 7.4% in 2005. This decrease was primarily due to the decline in gross margin, partially offset by a decline in SG&A expenses as a percentage of net sales to 26.7% in 2006 from 27.7% in 2005.

Table of Contents

Net Income. Net income increased $2.2 million to $12.9 million in 2006 from $10.7 million in 2005, but declined as a percentage of net sales to 3.9% in 2006 from 4.4% in 2005. Our effective income tax rate was approximately 38.8% for 2006 compared to 39.3% for 2005, reflecting slight variances in state income tax rates.

Year Ended December 31, 2005 Compared to Year Ended December 31, 2004

Net Sales. Net sales increased $73.2 million, or 43%, to $244.9 million in 2005 from $171.8 million in 2004. This increase was primarily driven by an increase of $32.6 million, or 19.0%, in comparable store sales, and also by additional non-comparable store sales of $18.3 million at the 17 stores opened during 2004 and $22.2 million at the 19 new stores opened during 2005. Comparable store sales increases were driven principally by maturation of new stores, expansion of our product mix and increased traffic across our store base. The average retail price per unit sold also increased slightly. Overall net sales increased due principally to the following factors:

- In 2005, we introduced several new product lines of prefinished hardwoods by Dura-Wood, which we believe customers choose more often in lieu of unfinished hardwoods that carry a lower average unit retail price. In addition, we increased our emphasis on selling add-on moldings and accessories, and the percentage of our net sales represented by those products increased from 5% in 2004 to 7% in 2005.

- Increases in comparable store sales and non-comparable net sales also resulted from the continuing maturation of our store base, as net sales at stores open for less than 36 months (67% of our stores in operation as of December 31, 2005) increase faster than our more mature stores.

Gross Profit and Gross Margin. Gross profit increased $30.2 million, or 54%, to $86.1 million in 2005 from $55.9 million in 2004, principally as a result of increases in net sales primarily due to higher sales volumes, the mix of sales and lower average supplier costs. Gross margin increased approximately 260 basis points to 35.2% in 2005 from 32.5% in 2004, which was principally due to the following factors:

- As part of our effort to optimize our sales mix, we increased sales of add-on moldings and accessories (products that generally have a higher gross margin than that our average product) to 7% in 2005 from lower levels in 2004, which resulted in an approximately 110 basis point increase in our gross margin.

- We relocated our distribution and Bellawood finishing facility, and our headquarters, to Toano, which enabled us to significantly lower finishing costs. The new finishing line also enabled us to take advantage of our increased finishing capacity by allowing us to purchase larger volumes of merchandise, which we believe generally enabled us to lower vendor costs. Taken together, the relocation resulted in an approximately 85 basis point increase in our gross margin.

- By increasing our product range, for example through the introduction of additional products in our Dura-Wood line, we were able to shift customers into choosing our premium prefinished products in lieu of lower margin alternatives such as unfinished products, which resulted in an approximately 50 basis point increase in our gross margin.

- Lower domestic and international transportation costs, resulting primarily from lower fuel costs, also caused an increase in gross margin.

Table of Contents

Operating Income. Operating income increased $11.0 million, or 154%, to $18.2 million in 2005, principally as a result of the $30.2 million increase in gross profit that was partially offset by a $19.4 million increase in SG&A expenses principally due to the following factors:

Advertising expenses increased $7.5 million, or 37%, in 2005 primarily due to the expansion of the national advertising branding campaign through television, radio and sports. As a percentage of net sales, advertising expenses declined to 11.3% in 2005 from 11.7% in 2004, principally due to our ability to leverage our national advertising over increased net sales.

Salaries, commissions and benefits increased $5.8 million, or 33%, in 2005 primarily due to the increase in the number of stores. As a percentage of net sales, salaries, commissions and benefits paid to our employees declined to 9.6% in 2005 from 10.2% in 2004, principally due to our ability to leverage our store support infrastructure over increased net sales.

Occupancy costs increased $2.8 million, or 54%, in 2005 principally due to 19 new stores opened in 2005, the full-year impact of 17 stores opened in 2004 and the opening of our new Toano facility in 2005. As a percentage of net sales, occupancy costs increased to 3.3% in 2005 from 3.0% in 2004.

Stock-based compensation expense increased to $3.3 million, or 1.3% of net sales in 2005, from $3.0 million, or 1.8% of net sales in 2004, primarily due to the amendment of Kevin s agreement with Tom.

As a percentage of net sales, operating income increased to 7.4% in 2005 from 4.2% in 2004. This increase was primarily due to the increase in gross margin for the reasons described above and a decline in SG&A expenses as a percentage of net sales to 27.7% in 2005 from 28.2% in 2004.

Net Income. Net income increased $2.7 million to $10.7 million in 2005 from $8.0 million in 2004, but declined as a percentage of net sales to 4.4% in 2005 from 4.6% in 2004, although pre-tax income increased to 7.2% of net sales in 2005 from 3.8% in 2004. Our effective income tax rate for 2005 was approximately 39.3%. Effective December 1, 2004, we elected to be taxed as a C corporation for federal and state income tax purposes. The effect of initially recognizing deferred tax assets and liabilities related to this change in tax status was included in the provision for income taxes for 2004. We were not subject to federal and certain state income taxes at the corporation level prior to that election.

Table of Contents

Quarterly Results and Seasonality

The following table sets forth our unaudited quarterly results of operations for 2005, 2006 and the first quarter of 2007, and quarterly results as a percentage of our annual results for 2005 and 2006. The information for each of these periods has been prepared on the same basis as the audited financial statements included elsewhere in this prospectus. This information includes all adjustments, which consist only of normal and recurring adjustments, management considers necessary for the fair presentation of such data. This data should be read in conjunction with the audited financial statements included elsewhere in this prospectus. The results of operations for historical periods are not necessarily indicative of results for any future period.

	2005 Quarter Ended (unaudited)					2006 Quarter Ended (unaudited)					2007 Quarter Ended (unaudited)
	Mar. 31,	June 30,	Sept. 30,	Dec. 31,	Total	Mar. 31,	June 30,	Sept. 30,	Dec. 31,	Total	Mar. 31,
	(in millions)					(in millions)					(in millions)
Net sales	$ 50.8	$ 61.6	$ 63.2	$ 69.3	$ 244.9	$ 76.1	$ 88.1	$ 83.1	$ 84.8	$ 332.1	$ 92.0
Gross profit	18.0	21.2	22.4	24.5	86.1	26.4	29.5	27.4	26.8	110.1	30.6
Operating income	3.5	5.5	5.7	3.5	18.2	5.9	8.0	4.8	2.7	21.4	3.8
Net income	2.1	3.2	3.3	2.1	10.7	3.6	4.8	2.9	1.6	12.9	2.2

	2005 Quarter Ended (unaudited)				2006 Quarter Ended (unaudited)			
	Mar. 31,	June 30,	Sept. 30,	Dec. 31,	Mar. 31,	June 30,	Sept. 30,	Dec. 31,
	(% of annual amount)				(% of annual amount)			
Net sales	20.7%	25.2%	25.8%	28.3%	22.9%	26.5%	25.0%	25.6%
Gross profit	20.9%	24.6%	26.0%	28.5%	24.0%	26.8%	24.9%	24.3%
Operating income	19.2%	30.2%	31.3%	19.3%	27.6%	37.4%	22.4%	12.6%
Net income	19.6%	29.9%	30.8%	19.7%	27.9%	37.2%	22.5%	12.4%

Our quarterly results of operations fluctuate depending on the timing of our advertising expenses and the timing of and income contributed by new stores. Our performance has also been impacted by certain of our initiatives to improve our infrastructure and to position our business to support sustainable growth and profitability in the future, including in particular the hiring of additional management personnel in the second half of 2006, as well as the steps we took to optimize inventory levels in the fourth quarter of 2006.

Our net sales also fluctuate slightly as a result of seasonal factors. We experience slightly higher net sales in spring and fall, when more home remodeling and home building activities are taking place, and slightly lower net sales in holiday periods and during the hottest summer months. These seasonal fluctuations, however, are minimized to some extent by our national presence, as markets experience different seasonal characteristics.

Liquidity and Capital Resources

We have historically funded our operations primarily through cash flows from operations and short-term and long-term borrowings under our senior secured loan agreement. Historically, our principal liquidity requirements have been to meet our working capital and capital expenditure needs.

Table of Contents

Our principal sources of liquidity as of March 31, 2007 consisted of $5.1 million in cash and cash equivalents and $7.8 million of availability under our $10.0 million revolving credit facility included within our senior secured loan agreement, reflecting $2.2 million for outstanding letters of credit and $0.02 million drawn under our operating line of credit.

We will use proceeds from this offering to repay all amounts outstanding under our senior secured loan agreement, including both our revolving credit facility and our separate term loan (approximately $10.8 million in aggregate as of May 31, 2007). We will use the remainder of the proceeds for general corporate purposes, including providing additional long-term capital to support the growth of our business (primarily through opening new stores) and maintaining our existing stores.

Cash and Cash Equivalents

During the three months ended March 31, 2007, cash and cash equivalents increased $1.2 million primarily due to $3.3 million of cash provided by operating activities, offset by $1.2 million used to repay long-term debt outstanding under our senior secured loan agreement and $0.8 million of cash used to purchase property and equipment. During the three months ended March 31, 2006, cash and cash equivalents increased $3.4 million primarily due to $3.6 million of cash provided by operating activities and borrowings of $0.7 million under our senior secured loan agreement, offset by $0.6 million of cash used to purchase property and equipment and $0.3 million of cash to repay long-term debt outstanding under our senior secured loan agreement.

The primary contributors to the decrease in cash and cash equivalents during 2006 were the use of $2.7 million of cash for purchases of property and equipment and $1.8 million of cash to repay scheduled long-term debt outstanding under the term-loan portion of our senior secured loan agreement, partially offset by $1.4 million of cash provided by operating activities and borrowings of $1.5 million under our revolving loan agreement. In 2005, cash and cash equivalents increased $3.0 million, to $6.0 million, from $3.0 million at the end of 2004. The primary contributor to the increase in cash and cash equivalents during 2005 was $8.0 million of cash provided by operating activities and borrowings of $2.1 million under our senior secured loan agreement, partially offset by the use of $4.3 million of cash for purchases of property and equipment and $3.0 million of cash to repay long-term debt outstanding under our senior secured loan agreement.

Cash Flows

Operating Activities. Net cash provided by operating activities was $3.3 million for the three months ended March 31, 2007 and $3.6 million for the three months ended March 31, 2006. Net cash provided by operating activities decreased in the first quarter of 2007 compared to the first quarter of 2006 primarily due to normal inventory purchases, fewer of which were financed through accounts payable to vendors for the three months ended March 31, 2007.

Net cash provided by operating activities was $1.4 million for 2006, $8.0 million for 2005 and $6.1 million for 2004. Net cash provided by operating activities decreased in 2006 compared to 2005 primarily because of increased inventory levels, partially offset by growth in net income and increases in accounts payable. The increase in inventory levels and increases in accounts payable resulted from our need to support additional sales from newly opened stores and increasing comparable store sales. In addition, we increased inventory, primarily in our Toano distribution facility, to be in a better position to drive sales and meet customer demand. Net cash provided by operating activities increased in 2005 compared to 2004 because of the growth in net income and increases in customer deposits, partially offset by decreases in accounts payable resulting from changing inventory levels, in part relating to discounted year-end purchases to take advantage of year-end supplier discounts which were particularly available in 2005.

Table of Contents

Investing Activities. Net cash used in investing activities was $0.8 million for the three months ended March 31, 2007 and $0.6 million for the three months ended March 31, 2006. Net cash used in investing activities during 2007 primarily related to routine capital purchases of computer hardware and software. Net cash used in investing activities during 2006 primarily related to upgrading of our telephone system and website.

Net cash used in investing activities was $2.7 million for 2006, $4.3 million for 2005 and $7.6 million for 2004. Net cash used in investing activities in 2006 primarily related to information technology (IT) systems, including new hardware and upgrades to our telephone system and website, as well as new store capital needs (primarily forklifts, store fixtures and leasehold improvements). In 2006, we slowed the increase in new store locations as we expanded our store support infrastructure to better facilitate sustainable growth of our operations. Net cash used in investing activities in 2005 primarily related to purchases of truck trailers that we use to move our merchandise from our warehouse to our stores and IT system maintenance, as well as new store capital needs. Net cash used in investing activities in 2004 primarily related to the completion of our finishing line in Toano, the purchase of truck trailers, the acquisition of Hardwood Holdings, LLC and new store capital needs and similar capital needs at our Toano facility.

We expect that our capital expenditures for 2007 will be approximately $7.0 million, relating primarily to store fixtures and leasehold improvements for new stores, as well as additional trailers, upgrades to our finishing line and IT costs relating to our new point-of-sale system, maintenance and our website. We had opened seven new store locations through May 31, 2007, and we intend to open a total of at least 25 new stores in 2007 and between 30 and 40 new stores during each of the next several years thereafter. We believe that our cash flow from operations, together with our existing liquidity sources and the net proceeds from this offering, will be sufficient to fund our operations and anticipated capital expenditures over at least the next 24 months.

Financing Activities. Net cash (used in) provided by financing activities was $(1.3) million for the three months ended March 31, 2007 and $0.3 million for the three months ended March 31, 2006. Net cash used in financing activities for 2007 was primarily attributable to principal payments on our senior loan agreements and capital lease obligations. Net cash was provided by financing activities in the first quarter of 2006 as we entered into the senior secured loan agreement in March 2006, partially offset by principal payments under the previous loan agreement.

Net cash (used in) provided by financing activities was $(0.8) million for 2006, $(0.7) million for 2005 and $1.4 million for 2004. Net cash used in financing activities for 2006 was primarily attributable to the use of $1.8 million to make principal payments on our senior secured loan agreement, partially offset by an increase of $1.5 million in borrowings. Net cash used in financing activities during 2005 was primarily attributable to principal payments on our senior loan agreements, partially offset by an increase of $2.1 million in borrowings. Net cash used in financing activities during 2004 was primarily attributable to the distribution of $42.6 million to Tom Sullivan in that year, including $12.6 million of distributions primarily related to our status as an S corporation and a $30.0 million distribution related to the sale of the preferred stock, partially offset by an increase of $35.0 million reflecting the proceeds from the sale of preferred stock to TA Associates and an increase of $11.9 million in borrowings under senior loan agreements and our equipment-related line of credit.

Senior Secured Loan Agreement

In March 2006, we entered into an amended and restated senior secured loan agreement with Bank of America, N.A. (Lender), which was amended in July 2006 to increase the size of the revolving credit facility. Under the agreement, we have a term loan with an original principal amount of $9.9 million and a revolving credit facility of up to $10.0 million. We are required to repay the principal amount under the

Table of Contents

term loan in 60 equal monthly installments with the first payment due on April 1, 2006 and the final payment due on March 1, 2011. The revolving credit facility expires on May 31, 2008.

Both the revolving credit facility and the term loan bear interest on the outstanding balance at a per annum rate equal to the Base Rate (generally equal to one-month LIBOR, subject to adjustments in certain circumstances) plus the Applicable Margin (as defined in the facility). The Applicable Margin depends on the Funded Debt to EBITDAR Ratio (as defined in the facility), and can range from 0.45% to 1.15% so long as the Base Rate is linked to one-month LIBOR. As of December 31, 2006 and March 31, 2007, the Applicable Margin was 0.90%, and the rate at which we accrued interest was 6.2%. We are required to pay an unused commitment fee of 0.25% per annum on undrawn amounts under the revolving credit facility.

The senior secured loan agreement and related security agreement contain a number of restrictions that will require us to maintain certain financial ratios and limit our ability, among other things, to borrow money, pledge our inventory or other assets as security in other borrowings or transactions, undergo a merger or consolidation, guarantee certain obligations of third parties, make or extend credit other than on ordinary terms in the course of our business or engage in any activity not reasonably related to those we presently conduct. We were in compliance with all of our covenants under the loan agreement as of December 31, 2006 and March 31, 2007. As of December 31, 2006 and March 31, 2007, we had remaining obligations of $9.1 and $7.9 million, respectively, to repay amounts outstanding under the loan agreement.

Issuance of Preferred Stock

In December 2004, funds managed by TA Associates purchased 7,952,018 shares of series A convertible preferred stock, par value $0.01, for $35.0 million. In connection with this sale, we declared a 150,000:1 common stock dividend to increase the number of common shares held by Tom from 100 to approximately 15.0 million. The stock split was effected in order to ensure that Tom would continue to hold an appropriate percentage of our common stock upon conversion of the convertible preferred stock held by TA Associates on a 1 for 1 basis. We distributed $42.6 million in cash to Tom in 2004, including $30.0 million of the proceeds from the sale of the convertible preferred stock (which represented a significant dilution of his ownership interest), $5.0 million to enable him to pay taxes on deemed income during the period we were an S corporation and $7.6 million of additional cash. We retained $5.0 million of cash from the sale of our Series A convertible preferred stock for general working capital purposes and to provide operating liquidity. As a result of those cash distributions, we had a total stockholder s deficit of $30.2 million as of December 31, 2004, which has steadily improved to a stockholder s deficit of $2.8 million as of March 31, 2007. In connection with this offering, TA Associates has agreed to convert all of the outstanding shares of series A convertible preferred stock that it holds into shares of common stock. For additional information about the investment by TA Associates, see Certain Relationships and Related Party Transactions Investment by TA Associates.

Related Party Transactions

Tom Sullivan is the sole owner of ANO LLC, DORA Real Estate Company, LLC and Wood on Wood Road, Inc., and he has a 50% membership interest in BMT Holdings, LLC (collectively, ANO and Related Companies). We leased our Toano facility, which includes a store location, and 25, 22 and 12 of our other store locations from these entities as of December 31, 2006, 2005 and 2004, representing 28.6%, 30.3% and 22.8% of total store leases, respectively. As of May 31, 2007, we leased our Toano facility and 26 of our other store locations from these entities, representing 27% of total store leases. The operating lease for our Toano facility has a base period through December 31, 2019. See Certain Relationships and Related Party Transactions.

Table of Contents

Contractual Commitments and Contingencies

Our significant contractual obligations and commitments as of December 31, 2006 and March 31, 2007 are summarized in the following tables:

		Payments Due by Period			
	Total	Less Than 1 Year	1 to 3 Years	3 to 5 Years	5+ Years
			(in thousands)		
Contractual obligations(1)					
As of December 31, 2006					
Debt obligations	$ 9,283	$ 2,804	$ 4,009	$ 2,470	$
Variable rate interest on debt obligations(2)	1,127	463	556	108	
Operating lease obligations(3)	31,384	5,548	9,463	5,531	10,842
Capital lease obligations, including interest(3)	330	269	61		
Supplier purchase commitments(4)	68,185	11,560	42,798	13,827	
Total contractual obligations	$ 110,309	$ 20,644	$ 56,887	$ 21,936	$ 10,842

		Payments Due by Period			
	Total	Less Than 1 Year	1 to 3 Years	3 to 5 Years	5+ Years
			(in thousands)		
Contractual obligations(1)					
As of March 31, 2007					
Debt obligations	$ 8,048	$ 2,076	$ 3,996	$ 1,976	$
Variable rate interest on debt obligations(5)	990	436	493	61	
Operating lease obligations(3)	33,401	6,004	10,006	5,738	11,653
Capital lease obligations, including interest(3)	243	211	32		
Supplier purchase commitments(4)	66,070	12,430	39,882	13,758	
Total contractual obligations	$ 108,752	$ 21,157	$ 54,409	$ 21,533	$ 11,653

(1) This table excludes the $35.0 million redemption amount of our series A convertible preferred stock. This table includes amounts outstanding under our term loan, in accordance with its maturity schedule, as set forth in our senior secured loan agreement. Upon consummation of this offering, the term loan will be repaid in full.

(2) As of December 31, 2006, our senior secured loan agreement accrued interest at a rate of one-month LIBOR plus 0.90%, and the rate at which we accrued interest was 6.2%. We estimated our obligation under this agreement by assuming that interest will accrue at the December 31, 2006 rate until the loan agreement expires.

(3) Included in this table is the base period or current renewal period for our operating leases. We lease certain buildings and equipment under non-cancelable operating leases and certain transportation equipment under non-cancelable capital leases. The leases expire at various dates through 2012 (2019 in the case of the lease for our Toano facility). The operating leases generally contain renewal provisions for varying periods of time.

(4) We have one long-term purchase agreement with a merchant vendor that we entered into in July 2006 that requires us to purchase approximately 27 million square feet of product over a four-year period ending August 2010. The agreement provides for a set menu of products, including prices and specifications, from which we can pick in placing our orders, and provides for a detailed process by which either party can request a change in prices or specifications, or add or delete products from the menu. In the table above, our commitment for less than one year was calculated using actual purchase commitments, while the commitment for subsequent years was calculated using our actual commitments, where applicable, plus our estimated remaining commitments under that agreement.

47

Table of Contents

(5) As of March 31, 2007, our senior secured loan agreement accrued interest at a rate of one-month LIBOR plus 0.90%, and the rate at which we accrued interest was 6.2%. We estimated our obligation under this agreement by assuming that interest will accrue at the March 31, 2007 rate until the loan agreement expires.

Off-Balance Sheet Arrangements

We currently do not have any off-balance sheet arrangements or other financing activities with special-purpose entities.

Qualitative and Quantitative Disclosures About Market Risk

Interest Rates. Because our senior secured loan agreement bears interest at a variable rate, we are exposed to market risks relating to changes in interest rates. Both the revolving portion of this facility and the term loan, which we expect to repay in full upon completion of this offering, bear interest at a variable rate, adjusted annually, based on our performance under certain specified operating ratios. From inception at March 23, 2006 to March 31, 2007, these loans bore interest at a per annum rate equal to one-month LIBOR plus 0.90%. A hypothetical 100 basis-point increase from the current interest level on $7.9 million, the amount outstanding under our existing revolving facility and our term facility at March 31, 2007, would result in approximately a $0.1 million increase in interest expense over a one-year period. A hypothetical 100 basis-point decrease from the current interest level would result in approximately a $0.1 million decrease in interest expense over a one-year period. We currently do not engage in any interest rate hedging activity and currently have no intention to do so in the foreseeable future. However, in the future, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Inflation

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

Critical Accounting Policies and Estimates

Critical accounting policies are those that we believe are both significant and that require us to make difficult, subjective or complex judgments, often because we need to estimate the effect of inherently uncertain matters. We base our estimates and judgments on historical experiences and various other factors that we believe to be appropriate under the circumstances. Actual results may differ from these estimates, and we might obtain different estimates if we used different assumptions or conditions. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our financial statements:

Recognition of Net Sales

We recognize net sales for products purchased at the time the customer takes possession of the merchandise. We recognize service revenue, which consists primarily of freight charges for in-home delivery, when the service has been rendered. Net sales are reduced by an allowance for anticipated sales returns that we estimate based on historical sales trends and experience. Any reasonably likely changes that may occur in the assumptions underlying our allowance estimates would not be expected to have a material impact on our financial condition or operating performance. In addition, customers who do not take immediate delivery of their purchases are generally required to leave a deposit of up to 50% of the sales amount with the balance payable when the products are delivered. These customer deposits benefit our cash flow and return on investment capital, since we receive partial payment for our customers purchases immediately. We record these deposits as a liability on our balance sheet under the line item Customer Deposits and Store Credits until the customer takes possession of the merchandise.

Equity Compensation

We maintain several equity incentive plans under which we may grant non-qualified stock options and incentive stock options to employees and non-employee directors. Using the prospective-transition method, we adopted the provisions of SFAS 123 (R) effective January 1, 2006. Prior to the adoption of SFAS 123 (R), we used the intrinsic value method under the provisions of Accounting Principles Board Opinion No. 25 (or APB 25). There were no material differences in the calculations of stock-based compensation expense under APB 25 and SFAS 123, Accounting for Stock-Based Compensation in 2005 or 2004. We recognize expense for our stock-based compensation based on the fair value of the awards that are granted. Measured compensation cost is recognized ratably over the service period of the related stock-based compensation award.

The fair value of stock options was estimated at the date of grant using the Black-Scholes-Merton valuation model. In order to determine the related stock compensation expense, we used the following assumptions:

Expected life of 7.5 years;

Expected stock price volatility of 35%, based on the median volatility of companies in a peer group;

Risk-free interest rates from 4.6% to 5.2%; and

Dividends are not expected to be paid in any year.

In addition, we are party to a stock-based agreement between Tom Sullivan and Kevin Sullivan, pursuant to which we generally guarantee Tom s cash payment obligation under the agreement. We account for that agreement as a variable performance plan. Under that agreement, as amended in August 2005, Kevin has the right to a fixed ownership percentage of Lumber Liquidators, Inc. on a fully diluted basis, plus an additional ownership percentage based on certain performance criteria (primarily a comparison of the net income of the region under his management to our total net income on a trailing twelve-month basis). In order to determine the compensation expense to be recor