INTERFACE INC
Form 10-K
February 28, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended December 30, 2012

Commission File No.: 001-33994

Interface, Inc.

(Exact name of registrant as specified in its charter)

Georgia	**58-1451243**
(State of incorporation)	**(I.R.S. Employer Identification No.)**

2859 Paces Ferry Road, Suite 2000

Atlanta, Georgia	**30339**
(Address of principal executive offices)	**(zip code)**

Registrant s telephone number, including area code: (770) 437-6800

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered:
Common Stock, $0.10 Par Value Per Share	**Nasdaq Global Select Market**
Series B Participating Cumulative Preferred Stock Purchase Rights	**Nasdaq Global Select Market**

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES x NO ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES ¨ NO x

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Date File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such

files). YES x NO ¨

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and a smaller reporting company in Rule 12b-2 of the Securities Exchange Act of 1934. (Check one):

Large Accelerated Filer x	Accelerated Filer ¨
Non-Accelerated Filer ¨	Smaller Reporting Company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO x

Aggregate market value of the voting and non-voting stock held by non-affiliates of the registrant as of June 29, 2012: $863,041,119 (63,319,231 shares valued at the last sales price of $13.63 on June 29, 2012). See Item 12.

Number of shares outstanding of each of the registrant s classes of Common Stock, as of February 15, 2013:

Class	Number of Shares
Common Stock, $0.10 par value per share	66,173,420

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2013 Annual Meeting of Shareholders are incorporated by reference into Part III.

PART I

ITEM 1. BUSINESS

Introduction and General

We are a worldwide leader in design, production and sales of modular carpet, also known as carpet tile. In recent years, modular carpet sales growth in the floorcovering industry has significantly outpaced the growth of the overall industry, as architects, designers and end users increasingly recognized the unique and superior attributes of modular carpet, including its dynamic design capabilities, greater economic value (which includes lower costs as a result of reduced waste in both installation and replacement), and installation ease and speed.

As a global company with a reputation for high quality, reliability and premium positioning, we market modular carpet in over 110 countries under the established brand names *Interface*® and *FLOR*®. Our principal geographic markets are the Americas, Europe and Asia-Pacific, where the percentages of our total net sales were approximately 55%, 30% and 15%, respectively, for fiscal year 2012.

Capitalizing on our leadership in modular carpet for the corporate office segment, we are executing a market diversification strategy to increase our presence and market share for modular carpet in non-corporate office market segments, such as government, education, healthcare, hospitality and retail space, which combined are almost twice the size of the approximately $1 billion U.S. corporate office market segment. Our diversification strategy also targets the approximately $11 billion U.S. residential market segment for carpet. As a result of our efforts, our mix of corporate office versus non-corporate office modular carpet sales in the Americas was 47% and 53%, respectively, for 2012. Company-wide, our mix of corporate office versus non-corporate office sales was 61% and 39%, respectively, in 2012. We believe the appeal and utilization of modular carpet is growing in each of these non-corporate office market segments, and we are using our considerable skills and experience with designing, producing and marketing modular products that make us the market leader in the corporate office segment to support and facilitate our penetration into these segments around the world.

In the first quarter of 2012, we committed to a new restructuring plan in our continuing efforts to reduce costs across our worldwide operations and more closely align our operations with reduced demand levels in certain markets. The plan primarily consisted of ceasing manufacturing and warehousing operations at our facility in Shelf, England. In connection with this restructuring plan, we incurred a pre-tax restructuring and asset impairment charge in the first quarter of 2012 in the amount of $16.3 million, as well as additional related charges of $0.8 million in the third quarter of 2012 and $2.3 million in the fourth quarter of 2012.

On July 20, 2012, a fire occurred at our manufacturing facility in Picton, Australia. The facility s carpet production line, primarily comprised of tufting and backing machinery, sustained extensive damage and was rendered inoperable. Other areas of the Picton site relating to yarn preparation and warehousing were largely undamaged by the fire. The finished goods inventory and some raw materials for the business are kept at a separate offsite location and were not affected by this incident. The Picton facility served our customers throughout Australia and New Zealand. It represented approximately 7% of our total annual production, 10% of our net sales, and 13% of our operating income. Since the fire, we have utilized adequate production capacity at our manufacturing facilities in Thailand, China and elsewhere to meet customer demand typically serviced from Picton. We have business interruption and property damage insurance. We are in the process of building a new manufacturing facility in Minto, Australia and expect it to become operational in late 2013.

In August of 2012, we sold our Bentley Prince Street business segment, which designed, manufactured and marketed high-end, designer-oriented broadloom and modular carpet. For additional information, please see Items 7 and 8 of this Annual Report.

Our Strengths

Our principal competitive strengths include:

Market Leader in Attractive Modular Carpet Segment. We are the world s leading manufacturer of carpet tile. Modular carpet has become more prevalent across all commercial interiors markets as designers, architects and end users have become more familiar with its unique attributes. We continue to drive this trend with our product innovations and designs discussed below. According to the 2012 *Floor Focus* interiors industry survey of the top 250 designers in the United States, carpet tile was ranked as the number one hot product for the eleventh consecutive year. We believe that we are well positioned to lead and capitalize upon the continued shift to modular carpet, both domestically and around the world.

Established Brands and Reputation for Quality, Reliability and Leadership. Our products are known in the industry for their high quality, reliability and premium positioning in the marketplace. Our established brand names in carpets are leaders in the industry. The 2012 *Floor Focus* survey ranked our *Interface* brand first or second in each of the survey categories of performance, service and design. On the international front, *Interface* and *Heuga*® are well-recognized brand names in carpet tiles for commercial, institutional and residential use. More generally, as the appeal and utilization of modular carpet continues to expand into market segments such as government, healthcare, education, hospitality, and retail and residential space, our reputation as the pioneer of modular carpet as well as our established brands and leading market position for modular carpet in the corporate office segment will enhance our competitive advantage in marketing to the customers in these new markets.

Innovative Product Design and Development Capabilities. Our product design and development capabilities have long given us a significant competitive advantage, and they continue to do so as modular carpet s appeal and utilization expand across virtually every market segment and around the globe. One of our best design innovations is our *i2* modular product line, which includes our popular *Entropy*® product for which we received a patent in 2005 on the key elements of its design. The *i2* line introduced and features mergeable dye lots, and includes carpet tile products designed to be installed randomly without reference to the orientation of neighboring tiles. The *i2* line offers cost-efficient installation and maintenance, interactive flexibility, and recycled and recyclable materials. Our *i2* line of products, which now comprises approximately 38% of our total U.S. modular carpet business, represents a differentiated category of smart, environmentally sensitive and stylish modular carpet, and *Entropy* has been the fastest growing product in our history. The award-winning design firm David Oakey Designs had a pivotal role in developing our *i2* product line, and our long-standing exclusive relationship with David Oakey Designs remains vibrant and augments our internal research, development and design staff. Another recent innovation is our patented *TacTiles*® carpet tile installation system, which uses small squares of adhesive plastic film to connect intersecting carpet tiles, thus eliminating the need for traditional carpet adhesive and resulting in a reduction in installation time and waste materials.

Made-to-Order and Global Manufacturing Capabilities. The success of our modernization and restructuring of operations over the past several years gives us a distinct competitive advantage in meeting two principal requirements of the specified products markets we primarily target that is, providing custom samples quickly and on-time delivery of customized final products. We also can generate realistic digital samples that allow us to create a virtually unlimited number of new design concepts and distribute them instantly for customer review, while at the same time reducing sampling waste. Approximately 75% to 80% of our modular carpet products in the United States and Asia-Pacific markets are now made-to-order, and we are increasing our made-to-order production in Europe as well. Our made-to-order capabilities not only enhance our marketing and sales, they significantly improve our inventory turns. Our global manufacturing capabilities in modular carpet production are an important component of this strength, and give us an advantage in serving the needs of multinational corporate customers that require products and services at various locations around the world. Our manufacturing locations across four continents enable us to compete effectively with local producers in our international markets, while giving international customers more favorable delivery times and freight costs.

Recognized Global Leadership in Ecological Sustainability. Our long-standing goal and commitment to be ecologically sustainable that is, the point at which we are no longer a net taker from the earth and do no harm to the biosphere has emerged as a competitive strength for our business and remains a strategic initiative. It includes *Mission Zero*®, our global branding initiative, which represents our mission to eliminate any negative impact our companies may have on the environment by the year 2020. Our acknowledged leadership position and expertise in this area resonate deeply with many of our customers and prospects around the globe, and provide us with a differentiating advantage in competing for business among architects, designers and end users of our products, who increasingly make purchase decisions based on green factors. The 2012 *Floor Focus* survey, which named our Interface business the top among Green Leaders , found that 74% of the designers surveyed consider sustainability an added benefit and 23% consider it a make or break issue when deciding what products to recommend or purchase.

Strong Operating Leverage Position. Our operating leverage, which we define as our ability to realize profit on incremental sales, is strong and generally allows us to increase earnings at a higher rate than our rate of increase in net sales. Our operating leverage position is primarily a result of (1) the specified, high-end nature and premium positioning of our principal products in the marketplace, and (2) the mix of fixed and variable costs in our manufacturing processes that allow us to increase production of most of our products without significant increases in capital expenditures or fixed costs. For example, while net sales from our modular carpet increased from $646.2 million in 2005 to $930.7 million in 2007 (a period in which our industry and business were recovering from a prior downturn), our operating income from that segment increased from $77.4 million (12.0% of net sales) in 2005 to $133.7 million (14.4% of net sales) in 2007.

Experienced and Motivated Management and Sales Force. An important component of our competitive position is the quality of our management team and its commitment to developing and maintaining an engaged and accountable workforce. Our team is highly skilled and dedicated to guiding our overall growth and expansion into our targeted market segments, while maintaining our leadership in traditional markets and our high contribution margins. We utilize an internal marketing and predominantly commissioned sales force of approximately 630 experienced personnel, stationed at over 70 locations in over 30 countries, to market our products and services in person to our customers. Our incentive compensation and our sales and marketing training programs are tailored to promote performance and facilitate leadership by our executives both in strategic areas as well as the company as a whole.

Our Business Strategy and Principal Initiatives

Our business strategy is to continue to use our leading position in modular carpet and our product design and global made-to-order capabilities as a platform from which to drive acceptance of modular carpet products across several industry segments, while maintaining our leadership position in the corporate office market segment. We will seek to increase revenues and profitability by capitalizing on the above strengths and pursuing the following key strategic initiatives:

Continue to Penetrate Non-Corporate Office Market Segments. We will continue our strategic focus on product design and marketing and sales efforts for non-corporate office market segments such as government, education, healthcare, hospitality, retail and residential space. We began this initiative as part of our market diversification strategy in 2001 (when our initial objective was reducing our exposure to the more severe economic cyclicality of the corporate office segment), and it has become a principal strategy generally for growing our business and enhancing profitability. We have shifted our mix of corporate office versus non-corporate office modular carpet sales in the Americas to 47% and 53%, respectively, for fiscal 2012 from 64% and 36%, respectively, in fiscal 2001. To implement this strategy, we:

- introduced specialized product offerings tailored to the unique demands of these segments, including specific designs, functionalities and prices;
- created special sales teams dedicated to penetrating these segments at a high level, with a focus on specific customer accounts rather than geographic territories; and
- realigned incentives for our corporate office segment sales force generally in order to encourage their efforts, and where appropriate, to assist our penetration of these other segments.

As part of this strategy, our *FLOR* line of products focuses on the approximately $11 billion U.S. residential carpet market segment. These products were specifically created to bring high style modular carpet to the North American residential market. We offer *FLOR* directly and over the Internet, in a *FLOR* catalog and in our 18 *FLOR* retail stores, and we plan to add four or five more retail stores in 2013. *FLOR* is also offered by many specialty retailers and in a number of major retail catalogs. Through such direct and indirect retailing, *FLOR* sales have grown more than 100% from 2005 to 2012.

Penetrate Expanding Geographic Markets for Modular Products. The popularity of modular carpet continues to increase compared with other floorcovering products across most markets, internationally as well as in the United States. While maintaining our leadership in the corporate office segment, we will continue to build upon our position as the worldwide leader for modular carpet in order to promote sales in all market segments globally. A principal part of our international focus which utilizes our global marketing capabilities and sales infrastructure is the significant opportunities in several emerging geographic markets for modular carpet. Some of these markets, such as China, India and Eastern Europe, represent large and growing economies that are essentially new markets for modular carpet products. Others, such as Germany and Italy, are established markets that are transitioning to the use of modular carpet from historically low levels of penetration. Each of these emerging markets represents a significant growth opportunity for our modular carpet business.

Continue to Minimize Expenses and Invest Strategically. We have steadily trimmed costs from our operations for several years through multiple initiatives, which have made us leaner today and for the future. Our supply chain and other cost containment initiatives have improved our cost structure and yielded the operating efficiencies we sought. While we still seek to minimize our expenses in order to increase profitability, we will also take advantage of strategic opportunities to invest in systems, processes and personnel that can help us grow our business and increase profitability and value.

Sustain Leadership in Product Design and Development. As discussed above, our leadership position for product design and development is a competitive advantage and key strength. Our *i2* products and *TacTiles* installation system have confirmed our position as an innovation leader in modular carpet. We will continue initiatives to sustain, augment and capitalize upon that strength to continue to increase our market share in targeted market segments. Our *Mission Zero* global branding initiative, which draws upon and promotes our ecological sustainability commitment, is part of those initiatives and includes placing our *Mission Zero* logo on many of our marketing and merchandising materials distributed throughout the world.

Use Strong Free Cash Flow Generation to De-leverage Our Balance Sheet. Our principal business has been structured including through our rationalization and repositioning initiatives to yield high contribution margins and generate strong free cash flow (by which we mean cash available to apply towards debt service and potential stock repurchases, strategic acquisitions and the like). Our historical investments in global manufacturing capabilities and mass customization techniques and facilities, which we have maintained, also contribute to our ability to generate substantial levels of free cash flow. We will use our strong free cash flow generation capability to continue to repay debt and strengthen our financial position. We will also continue to execute programs to reduce costs further and enhance free cash flow. In addition, our existing capacity to increase production levels without significant capital expenditures will further enhance our generation of free cash flow as demand for our products rises.

Challenges

In order to capitalize on our strengths and to implement successfully our business strategy and the principal initiatives discussed above, we will have to handle successfully several challenges that confront us or that affect our industry in general. As discussed in the Risk Factors in Item 1A of this Report, several factors could make it difficult for us, including:

- sales of our principal products have been and may continue to be affected by adverse economic cycles in the renovation and construction of commercial and institutional buildings;

- we compete with a large number of manufacturers in the highly competitive commercial floorcovering products market, and some of these competitors have greater financial resources than we do;

- our success depends significantly upon the efforts, abilities and continued service of our senior management executives and our principal design consultant, and our loss of any of them could affect us adversely;

- our substantial international operations are subject to various political, economic and other uncertainties that could adversely affect our business results;

- large increases in the cost of petroleum-based raw materials could adversely affect us if we are unable to pass these cost increases through to our customers;

- unanticipated termination or interruption of any of our arrangements with our primary third party suppliers of synthetic fiber could have a material adverse effect on us; and

- we have a significant amount of indebtedness, which could have important negative consequences to us.

We believe our business model is strong enough, and our strategic initiatives are properly calibrated, for us to handle these and other challenges we will encounter in our business.

Seasonality

Our first quarter has typically been our slowest quarter while our fourth quarter has typically been our best quarter, with sales generally increasing throughout the course of the fiscal year. However, in recent years, as our sales efforts and results in the education market segment (which has a heavy second quarter buying season) have increased, our second quarter sales have occasionally eclipsed our third or fourth quarter sales.

Our Products and Services

Modular Carpet

Interface is the world s largest manufacturer and marketer of modular carpet. Our modular carpet system, which is marketed under the established global brands *Interface* and *Heuga,* utilizes carpet tiles cut in precise, dimensionally stable squares (usually 50 cm x 50 cm) or rectangles to produce a floorcovering that combines the appearance and texture of traditional soft floorcovering with the advantages of a modular carpet system. Our *GlasBac*® technology employs a fiberglass-reinforced polymeric composite backing that provides dimensional stability and reduces the need for adhesives or fasteners. We also make carpet tiles with a backing containing post-industrial and/or post-consumer recycled materials, which we market under the *GlasBacRE* brand. In 2008, we introduced the *Convert* collection of carpet tile designed and manufactured with yarn containing varying degrees of post-consumer nylon, depending on the style and color. We received the 2012 and 2011 Best of NeoCon Silver Awards in the modular carpet category for our *Urban Retreat* and *Luxe at Work* Collections, respectively.

Our carpet tile has become popular for a number of reasons. Carpet tile incorporating our reinforced backing may be easily removed and replaced, permitting rearrangement of furniture without the inconvenience and expense associated with removing, replacing or repairing other soft surface flooring products, including broadloom carpeting. Because a relatively small portion of a carpet installation often receives the bulk of traffic and wear, the ability to rotate carpet tiles between high traffic and low traffic areas and to selectively replace worn tiles can significantly increase the average life and cost efficiency of the floorcovering. In addition, carpet tile facilitates access to sub-floor air delivery systems and telephone, electrical, computer and other wiring by lessening disruption of operations. It also eliminates the cumulative damage and unsightly appearance commonly associated with frequent cutting of conventional carpet as utility connections and disconnections are made. We believe that, within the overall floorcovering market, the worldwide demand for modular carpet is increasing as more customers recognize these advantages.

We use a number of conventional and technologically advanced methods of carpet construction to produce carpet tiles in a wide variety of colors, patterns, textures, pile heights and densities. These varieties are designed to meet both the practical and aesthetic needs of a broad spectrum of commercial interiors particularly offices, healthcare facilities, airports, educational and other institutions, hospitality spaces, and retail facilities and residential interiors. Our carpet tile systems permit distinctive styling and patterning that can be used to complement interior designs, to set off areas for particular purposes and to convey graphic information. While we continue to manufacture and sell a substantial portion of our carpet tile in standard styles, an increasing percentage of our modular carpet sales is custom or made-to-order product designed to meet customer specifications.

In addition to general uses of our carpet tile, we produce and sell a specially adapted version of our carpet tile for the healthcare facilities market. Our carpet tile possesses characteristics such as the use of the *Intersept* antimicrobial, static-controlling nylon yarns, and thermally pigmented, colorfast yarns which make it suitable for use in these facilities in place of hard surface flooring. Moreover, we launched our *FLOR* line of products to specifically target modular carpet sales to the residential market segment. Through our relationship with David Oakey Designs, we also have created modular carpet products (some of which are part of our *i2* product line) specifically designed for each of the education, hospitality and retail market segments.

We also manufacture and sell two-meter roll goods that are structure-backed and offer many of the advantages of both carpet tile and broadloom carpet. These roll goods are often used in conjunction with carpet tiles to create special design effects. Our current principal customers for these products are in the education, healthcare and government market segments.

Broadloom Carpet

In August of 2012, we sold our Bentley Prince Street business segment to a third party. This business designed, manufactured and marketed high-end, designer-oriented broadloom and modular carpet for commercial and residential markets. As a result of this sale, we no longer have a presence in the broadloom carpet market.

Other Products and Services

We sell a proprietary antimicrobial chemical compound under the registered trademark *Intersept* that we incorporate in all of our modular carpet products and have licensed to another company for use in air filters. We also sell our *TacTiles* carpet tile installation system, along with a variety of traditional adhesives and products for carpet installation and maintenance that are manufactured by a third party. In addition, we continue to manufacture and sell our *Intercell*® brand raised/access flooring product in Europe. We also continue to provide turnkey project management services for national accounts and other large customers through our *InterfaceSERVICES* business.

Marketing and Sales

We have traditionally focused our carpet marketing strategy on major accounts, seeking to build lasting relationships with national and multinational end-users, and on architects, engineers, interior designers, contracting firms, and other specifiers who often make or significantly influence purchasing decisions. While most of our sales are in the corporate office segment, both new construction and renovation, we also emphasize sales in other segments, including retail space, government institutions, schools, healthcare facilities, tenant improvement space, hospitality centers, residences and home office space. Our marketing efforts are enhanced by the established and well-known brand names of our carpet products, including *Interface, FLOR* and *Heuga*. Our exclusive consulting agreement with the award-winning, premier design firm David Oakey Designs enabled us to introduce more than 20 new carpet designs in the United States in 2012 alone.

An important part of our marketing and sales efforts involves the preparation of custom-made samples of requested carpet designs, in conjunction with the development of innovative product designs and styles to meet the customer s particular needs. Our mass customization initiative simplified our carpet manufacturing operations, which significantly improved our ability to respond quickly and efficiently to requests for samples. In most cases, we can produce samples to customer specifications in less than five days, which significantly enhances our marketing and sales efforts and has increased our volume of higher margin custom or made-to-order sales. In addition, through our websites, we have made it easy to view and request samples of our products. We also have technology which allows us to provide digital, simulated samples of our products, which helps reduce raw material and energy consumption associated with our samples.

We primarily use our internal marketing and sales force to market our carpet products. In order to implement our global marketing efforts, we have product showrooms or design studios in the United States, Canada, Mexico, Brazil, Denmark, England, France, Germany, Spain, the Netherlands, India, Australia, Norway, United Arab Emirates, Russia, Singapore, Hong Kong, Thailand, China and elsewhere. We expect to open offices in other locations around the world as necessary to capitalize on emerging marketing opportunities.

We distribute our product through two primary channels. (1) direct sales to end users; and (2) indirect sales through independent contractors or distributors. In each case, we may also call upon architects, engineers, interior designers, contracting firms and other specifiers who often make or substantially influence purchasing decisions. In 2010, we entered into a new distribution arrangement with the Bravo Network, which is comprised of independent flooring distributors that provide distribution logistics throughout the United States. Under this arrangement, the Bravo Network offers an exclusive collection of 10 distinct styles of our carpet tile. The collection sold through the Bravo Network targets the industry s main street sector in the United States, comprised primarily of commercial customers purchasing non-specified products through flooring retail stores.

Manufacturing

We manufacture carpet at two locations in the United States and at facilities in the Netherlands, the United Kingdom, Thailand and China. Until July of 2012, we also manufactured carpet in Australia, but as a result of a fire this facility is no longer operational. We are in the process of building a new facility in Australia and expect it to become operational in late 2013.

Having foreign manufacturing operations enables us to supply our customers with carpet from the location offering the most advantageous delivery times, duties and tariffs, exchange rates, and freight expense, and enhances our ability to develop a strong local presence in foreign markets. We believe that the ability to offer consistent products and services on a worldwide basis at attractive prices is an important competitive advantage in servicing multinational customers seeking global supply relationships. We will consider additional locations for manufacturing operations in other parts of the world as necessary to meet the demands of customers in international markets.

To the extent practicable, we seek to standardize our worldwide modular carpet manufacturing procedures. In connection with the implementation of this plan, we strive to establish global standards for our tufting equipment, yarn systems and product styling. We previously had changed our standard carpet tile size to be 50 cm x 50 cm, which we believe has allowed us to reduce operational waste and fossil fuel energy consumption and to offer consistent product sizing for our global customers.

Our raw materials are generally available from multiple sources both regionally and globally with the exception of synthetic fiber (nylon yarn). For yarn, we principally rely upon two major global suppliers, but we also have significant relationships with at least two other suppliers. Although our number of principal yarn suppliers is limited, we do have the capability to manufacture carpet using face fiber produced from two separate polymer feedstocks nylon 6 and nylon 6,6 which provides additional flexibility with respect to yarn supply inputs, if needed. Our global sourcing strategy, including with respect to our principal yarn suppliers and dual polymer manufacturing capability, allows us to guard against any potential shortages of raw materials or raw material suppliers in a specific polymer supply chain.

We have a flexible-inputs carpet backing line, which we call *Cool Blue*, at our modular carpet manufacturing facility in LaGrange, Georgia. Using next generation thermoplastic technology, the custom-designed backing line dramatically improves our ability to keep reclaimed and waste carpet in the production technical loop, and further permits us to explore other plastics and polymers as inputs. We also have technology that more cleanly separates the face fiber and backing of reclaimed and waste carpet, thus making it easier to recycle some of its components and providing a purer supply of inputs for the *Cool Blue* process. This technology, which is part of our *ReEntry®2.0* carpet reclamation program, allows us to send some of the reclaimed face fiber back to our fiber supplier to be blended with virgin or other post-industrial materials and extruded into new fiber.

The environmental management systems of our floorcovering manufacturing facilities in LaGrange, Georgia, West Point, Georgia, Northern Ireland, the Netherlands and Thailand are certified under International Standards Organization (ISO) Standard No. 14001.

Our significant international operations are subject to various political, economic and other uncertainties, including risks of restrictive taxation policies, foreign exchange restrictions, changing political conditions and governmental regulations. We also receive a substantial portion of our revenues in currencies other than U.S. dollars, which makes us subject to the risks inherent in currency translations. Although our ability to manufacture and ship products from facilities in several foreign countries reduces the risks of foreign currency fluctuations we might otherwise experience, we also engage from time to time in hedging programs intended to further reduce those risks.

Competition

We compete, on a global basis, in the sale of our modular carpet products with other carpet manufacturers and manufacturers of vinyl and other types of floorcoverings, including broadloom carpet. Although the industry has experienced significant consolidation, a large number of manufacturers remain in the industry. We believe we are the largest manufacturer of modular carpet in the world. However, a number of domestic and foreign competitors manufacture modular carpet as one segment of their business, and some of these competitors have financial resources greater than ours. In addition, some of the competing carpet manufacturers have the ability to extrude at least some of their requirements for fiber used in carpet products, which decreases their dependence on third party suppliers of fiber.

We believe the principal competitive factors in our primary floorcovering markets are brand recognition, quality, design, service, broad product lines, product performance, marketing strategy and pricing. In the corporate office market segment, modular carpet competes with various floorcoverings, of which broadloom carpet is the most common. The quality, service, design, better and longer average product performance, flexibility (design options, selective rotation or replacement, use in combination with roll goods) and convenience of our modular carpet are our principal competitive advantages.

We believe we have competitive advantages in several other areas as well. First, our exclusive relationship with David Oakey Designs allows us to introduce numerous innovative and attractive carpet tile products to our customers. Additionally, we believe that our global manufacturing capabilities are an important competitive advantage in serving the needs of multinational corporate customers. We believe that the incorporation of the *Intersept* antimicrobial chemical agent into the backing of our modular carpet enhances our ability to compete successfully across all of our market segments generally, and specifically with resilient tile in the healthcare market.

In addition, we believe that our goal and commitment to be ecologically sustainable by 2020 is a brand-enhancing, competitive strength as well as a strategic initiative. Increasingly, our customers are concerned about the environmental and broader ecological implications of their operations and the products they use in them. Our leadership, knowledge and expertise in the area, especially in the green building movement and the related LEED certification program, resonate deeply with many of our customers and prospects around the globe, and these businesses are increasingly making purchase decisions based on green factors. Our modular carpet products historically have had inherent installation and maintenance advantages that translated into greater efficiency and waste reduction. We are using raw materials and production technologies, such as our *Cool Blue* backing line and our *ReEntry 2.0* reclaimed carpet separation process, that directly reduce the adverse impact of those operations on the environment and limit our dependence on petrochemicals.

Product Design, Research and Development

We maintain an active research, development and design staff of approximately 80 people and also draw on the research and development efforts of our suppliers, particularly in the areas of fibers, yarns and modular carpet backing materials. Our research and development costs were $12.4 million, $12.1 million and $11.1 million in 2012, 2011, and 2010, respectively.

Our research and development team provides technical support and advanced materials research and development for us. The team assisted in the development of our *NexStep*® backing, which employs moisture-impervious polycarbite precoating technology with a chlorine-free urethane foam secondary backing, and also helped develop a post-consumer recycled content, polyvinyl chloride, or PVC, extruded sheet process that has been incorporated into our *GlasBacRE* modular carpet backing. Our post-consumer recycled content PVC extruded sheet exemplifies our commitment to closing-the-loop in recycling. More recently, this team developed our patented *TacTiles* carpet tile installation system, which uses small squares of adhesive plastic film to connect intersecting carpet tiles. The team also helped implement our *Cool Blue* flexible inputs backing line and our *ReEntry 2.0* reclaimed carpet separation technology and post-consumer recycling technology for nylon face fibers. With a goal of supporting sustainable product designs in floorcoverings applications, we continue to evaluate renewable polymers for use in our products.

Our research and development team also is the coordinator of our QUEST and EcoSense initiatives (discussed below under Environmental Initiatives) and supports the dissemination, consultancies and technical communication of our global sustainability endeavors. This team also provides all biochemical and technical support to *Intersept* antimicrobial chemical product initiatives.

Innovation and increased customization in product design and styling are the principal focus of our product development efforts. Our carpet design and development team is recognized as an industry leader in carpet design and product engineering for the commercial and institutional markets.

David Oakey Designs provides carpet design and consulting services to us pursuant to a consulting agreement. David Oakey Designs services under the agreement include creating commercial carpet designs for use by our modular carpet businesses throughout the world, and overseeing product development, design and coloration functions for our modular carpet business in North America. The current agreement runs through April 2014. While the agreement is in effect, David Oakey Designs cannot provide similar services to any other carpet company. Through our relationship with David Oakey Designs, we introduced more than 20 new carpet designs in 2012 alone, and have enjoyed considerable success in winning U.S. carpet industry awards.

David Oakey Designs also contributed to our ability to efficiently produce many products from a single yarn system. Our mass customization production approach evolved, in major part, from this concept. In addition to increasing the number and variety of product designs, which enables us to increase high margin custom sales, the mass customization approach increases inventory turns and reduces inventory levels (for both raw materials and standard products) and their related costs because of our more rapid and flexible production capabilities.

Our *i2* product line which includes, among others, our patented *Entropy* modular carpet product represents an innovative breakthrough in the design of modular carpet. The *i2* line introduced and features mergeable dye lots, cost-efficient installation and maintenance, interactive flexibility and recycled and recyclable materials. Some of these products may be installed without regard to the directional orientation of the carpet tile, and their features also make installation, maintenance and replacement of modular carpet easier, less expensive and less wasteful.

Environmental Initiatives

In the latter part of 1994, we commenced a new industrial ecological sustainability initiative called EcoSense, inspired in part by the interest of customers concerned about the environmental implications of how they and their suppliers do business. EcoSense, which includes our QUEST waste reduction initiative, is directed towards the elimination of energy and raw materials waste in our businesses, and, on a broader and more long-term scale, the practical reclamation and ultimate restoration of shared environmental resources. The initiative involves a commitment by us:

- to learn to meet our raw material and energy needs through recycling of carpet and other petrochemical products and harnessing benign energy sources; and

- to pursue the creation of new processes to help sustain the earth s non-renewable natural resources.

We have engaged some of the world s leading authorities on global ecology as environmental advisors. The list of advisors includes: Paul Hawken, author of *The Ecology of Commerce: A Declaration of Sustainability* and *The Next Economy,* and co-author of *Natural Capitalism: Creating the Next Industrial Revolution;* Amory Lovins, energy consultant and co-founder of the Rocky Mountain Institute; John Picard, President of E2 Environmental Enterprises; Bill Browning, fellow and former director of the Rocky Mountain Institute s Green Development Services; Janine M. Benyus, author of *Biomimicry*; and Bob Fox, renowned architect.

Our leadership, knowledge and expertise in this area, especially in the green building movement and the related LEED certification program, resonate deeply with many of our customers and prospects around the globe, and these businesses are increasingly making purchase decisions based on green factors. As more customers in our target markets share our view that sustainability is good business and not just good deeds, our acknowledged leadership position should strengthen our brands and provide a differentiated advantage in competing for business.

To further raise awareness of our goal of becoming sustainable, we launched our *Mission Zero* global branding initiative, which represents our mission to eliminate any negative impact our companies may have on the environment by the year 2020. As part of this initiative, our *Mission Zero* logo appears on many of our marketing and merchandising materials distributed throughout the world.

Backlog

Our backlog of unshipped orders was approximately $108.4 million at February 15, 2013, compared with approximately $101.1 million at February 19, 2012. Historically, backlog is subject to significant fluctuations due to the timing of orders for individual large projects and currency fluctuations. All of the backlog orders at February 15, 2013 are expected to be shipped during the succeeding six to nine months.

Patents and Trademarks

We own numerous patents in the United States and abroad on floorcovering products and on manufacturing processes. The duration of United States patents is between 14 and 20 years from the date of filing of a patent application or issuance of the patent; the duration of patents issued in other countries varies from country to country. We maintain an active patent and trade secret program in order to protect our proprietary technology, know-how and trade secrets. Although we consider our patents to be very valuable assets, we consider our know-how and technology even more important to our current business than patents, and, accordingly, believe that expiration of existing patents or nonissuance of patents under pending applications would not have a material adverse effect on our operations.

We also own many trademarks in the United States and abroad. In addition to the United States, the primary countries in which we have registered our trademarks are the United Kingdom, Germany, Italy, France, Canada, Australia, Japan, and various countries in Central America, South America and Asia. Some of our more prominent registered trademarks include: *Interface, FLOR, Heuga, Intersept, GlasBac, Intercell,* and *Mission Zero.* Trademark registrations in the United States are valid for a period of 10 years and are renewable for additional 10-year periods as long as the mark remains in actual use. The duration of trademarks registered in other countries varies from country to country.

Financial Information by Operating Segments and Geographic Areas

The Notes to Consolidated Financial Statements appearing in Item 8 of this Report set forth information concerning our sales and long-lived assets by geographic areas. Following the sale of Bentley Prince Street, we have only one operating segment. Current and prior periods have been reclassified to include the results of operations and related disposal costs, gains and losses for the Bentley Prince Street business as discontinued operations. In addition, assets and liabilities of the Bentley Prince Street business have been reported in assets and liabilities held for sale for all reported periods.

Employees

At December 30, 2012, we employed a total of 3,146 employees worldwide. Of such employees, 1,748 were clerical, staff, sales, supervisory and management personnel and 1,398 were manufacturing personnel. We also utilized the services of 131 temporary personnel as of December 30, 2012.

Some of our production employees in Australia and the United Kingdom are represented by unions. In the Netherlands, a Works Council, the members of which are Interface employees, is required to be consulted by management with respect to certain matters relating to our operations in that country, such as a change in control of Interface Europe B.V. (our modular carpet subsidiary based in the Netherlands), and the approval of the Council is required for some of our actions, including changes in compensation scales or employee benefits. Our management believes that its relations with the Works Council, the unions and all of our employees are good.

Environmental Matters

Our operations are subject to laws and regulations relating to the generation, storage, handling, emission, transportation and discharge of materials into the environment. The costs of complying with environmental protection laws and regulations have not had a material adverse impact on our financial condition or results of operations in the past and are not expected to have a material adverse impact in the future. The environmental management systems of our floorcovering manufacturing facilities in LaGrange, Georgia, West Point, Georgia, Northern Ireland, the Netherlands and Thailand are certified under ISO Standard No. 14001.

Executive Officers of the Registrant

Our executive officers, their ages as of December 30, 2012, and their principal positions with us are set forth below. Executive officers serve at the pleasure of the Board of Directors.

Name	Age	Principal Position(s)
Daniel T. Hendrix	58	President and Chief Executive Officer
Robert A. Coombs	54	Senior Vice President (Asia-Pacific)
Patrick C. Lynch	43	Senior Vice President and Chief Financial Officer
Lindsey K. Parnell	55	Senior Vice President (Europe)
John R. Wells	51	Senior Vice President (Americas)
Raymond S. Willoch	54	Senior Vice President-Administration, General Counsel and Secretary

Mr. Hendrix joined us in 1983 after having worked previously for a national accounting firm. He was promoted to Treasurer in 1984, Chief Financial Officer in 1985, Vice President-Finance in 1986, Senior Vice President in October 1995, Executive Vice President in October 2000, and President and Chief Executive Officer in July 2001. He was elected to the Board in October 1996 and has served on the Executive Committee of the Board since July 2001. In October 2011, Mr. Hendrix was elected as Chairman of the Board of Directors.

Mr. Coombs originally worked for us from 1988 to 1993 as a marketing manager for our *Heuga* carpet tile operations in the United Kingdom and later for all of our European floorcovering operations. In 1996, Mr. Coombs returned to us as Managing Director of our Australian operations. He was promoted in 1998 to Vice President-Sales and Marketing, Asia-Pacific, with responsibility for Australian operations and sales and marketing in Asia, which was followed by a promotion to Senior Vice President, Asia-Pacific. He was promoted to Senior Vice President, European Sales, in May 1999 and Senior Vice President, European Sales and Marketing, in April 2000. In February 2001, he was promoted to President and Chief Executive Officer of Interface Overseas Holdings, Inc. with responsibility for all of our floorcoverings operations in both Europe and the Asia-Pacific region, and he became a Vice President of Interface. In September 2002, Mr. Coombs relocated back to Australia, retaining responsibility for our floorcovering operations in the Asia-Pacific region while Mr. Parnell (see below) assumed responsibility for floorcovering operations in Europe. Mr. Coombs was promoted to Senior Vice President of Interface in July 2008.

Mr. Lynch joined us in 1996 after having previously worked for a national accounting firm. He became Assistant Corporate Controller in 1998 and Assistant Vice President and Corporate Controller in 2000. Mr. Lynch was promoted to Vice President and Chief Financial Officer in July 2001. Mr. Lynch was promoted to Senior Vice President in March 2007.

Mr. Parnell was the Production Director for Firth Carpets (our former European broadloom operations) at the time it was acquired by us in 1997. In 1998, Mr. Parnell was promoted to Vice President, Operations for the United Kingdom, and in 1999 he was promoted to Senior Vice President, Operations for our entire European floorcovering division. In September 2002, he was promoted to President and Chief Executive Officer of our floorcovering operations in Europe, and became a Vice President of Interface in October 2002. Mr. Parnell was promoted to Senior Vice President of Interface in July 2008.

Mr. Wells joined us in February 1994 as Vice President-Sales of Interface Flooring Systems, Inc. (now InterfaceFLOR, LLC), our principal U.S. modular carpet subsidiary. Mr. Wells was promoted to Senior Vice President-Sales & Marketing of Interface Flooring Systems in October 1994. He was promoted to Vice President of Interface and President of Interface Flooring Systems in July 1995. In March 1998, Mr. Wells was also named President of both Prince Street Technologies, Ltd. and Bentley Mills, Inc. (our former U.S. broadloom operations), making him President of all three of our U.S. carpet mills at that time. In November 1999, Mr. Wells was named Senior Vice President of Interface, and President and Chief Executive Officer of Interface Americas Holdings, LLC (formerly Interface Americas, Inc.), thereby assuming operations responsibility for all of our floorcovering businesses in the Americas.

Mr. Willoch, who previously practiced with an Atlanta law firm, joined us in June 1990 as Corporate Counsel. He was promoted to Assistant Secretary in 1991, Assistant Vice President in 1993, Vice President in January 1996, Secretary and General Counsel in August 1996, and Senior Vice President in February 1998. In July 2001, he was named Senior Vice President-Administration and assumed corporate responsibility for various staff functions.

Available Information

We make available free of charge on or through our Internet website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Our Internet address is http://www.interface.com. The SEC maintains a website that contains annual, quarterly and current reports, proxy statements and other information that issuers (including the Company) file electronically with the SEC. The SEC s website is http://www.sec.gov.

Interface, Inc. was incorporated in 1973 as a Georgia corporation.

Forward-Looking Statements

This report on Form 10-K contains forward-looking statements within the meaning of the Securities Act of 1933, and the Securities Exchange Act of 1934, and the Private Securities Litigation Reform Act of 1995. Words such as believes, anticipates, plans, expects and similar expressions are intended to identify forward-looking statements. Forward-looking statements include statements regarding the intent, belief or current expectations of our management team, as well as the assumptions on which such statements are based. Any forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties that could cause actual results to differ materially from those contemplated by such forward-looking statements. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results over time. Important factors currently known to management that could cause actual results to differ materially from those in forward-looking statements include risks and uncertainties associated with economic conditions in the commercial interiors industry as well as the risks and uncertainties discussed below in Item 1A, Risk Factors .

ITEM 1A. RISK FACTORS

You should carefully consider the following factors, in addition to the other information included in this Annual Report on Form 10-K and the other documents incorporated herein by reference, before deciding whether to purchase or sell our common stock. Any or all of the following risk factors could have a material adverse effect on our business, financial condition, results of operations and prospects.

The ongoing worldwide financial and credit crisis could have a material adverse effect on our business, financial condition and results of operations.

The ongoing worldwide financial and credit crisis has reduced the availability of liquidity and credit to fund the continuation and expansion of many business operations worldwide. This shortage of liquidity and credit, combined with recent substantial losses in worldwide equity markets, could lead to a worldwide economic recession and result in a material adverse effect on our business, financial condition and results of operations. Specifically, the limited availability of credit and liquidity adversely affects the ability of customers and suppliers to obtain financing for significant purchases and operations. Consequently, customers may defer, delay or cancel renovation and construction projects where our carpet is used, resulting in decreased orders and sales for us, and they also may not be able to pay us for those products and services we already have provided to them. For the same reasons, suppliers may not be able to produce and deliver raw materials and other goods and services that we have ordered from them, thus disrupting our own manufacturing operations. In addition, our ability to obtain funding from capital markets may be severely restricted at a time when we would like, or need, to access those markets. This inability to obtain that funding could prevent us from pursuing important strategic growth plans, from reacting to changing economic and business conditions, and from refinancing existing debt (which in turn could lead to a default on our debt). The financial and credit crisis also could have an impact on the lenders under our credit facilities, causing them to fail to meet their obligations to provide us with loans and letters of credit, which are important sources of liquidity for us.

Our domestic revolving credit facility matures in June 2016 and our 7 5/8% Senior Notes mature in December 2018. We cannot assure you that we will be able to renegotiate or refinance this debt on commercially reasonable terms, or at all, especially given the ongoing worldwide financial and credit crisis.

Sales of our principal products have been and may continue to be affected by adverse economic cycles in the renovation and construction of commercial and institutional buildings.

Sales of our principal products are related to the renovation and construction of commercial and institutional buildings. This activity is cyclical and has been affected by the strength of a country s or region s general economy, prevailing interest rates and other factors that lead to cost control measures by businesses and other users of commercial or institutional space. The effects of cyclicality upon the corporate office segment tend to be more pronounced than the effects upon the institutional segment. Historically, we have generated more sales in the corporate office segment than in any other market. The effects of cyclicality upon the new construction segment of the market also tend to be more pronounced than the effects upon the renovation segment. These effects may recur and could be more pronounced if global economic conditions do not improve or are further weakened.

We compete with a large number of manufacturers in the highly competitive floorcovering products market, and some of these competitors have greater financial resources than we do.

The floorcovering industry is highly competitive. Globally, we compete for sales of floorcovering products with other carpet manufacturers and manufacturers of other types of floorcovering. Although the industry has experienced significant consolidation, a large number of manufacturers remain in the industry. Some of our competitors, including a number of large diversified domestic and foreign companies who manufacture modular carpet as one segment of their business, have greater financial resources than we do.

Our success depends significantly upon the efforts, abilities and continued service of our senior management executives and our principal design consultant, and our loss of any of them could affect us adversely.

We believe that our success depends to a significant extent upon the efforts and abilities of our senior management executives. In addition, we rely significantly on the leadership that David Oakey of David Oakey Designs provides to our internal design staff. Specifically, David Oakey Designs provides product design/production engineering services to us under an exclusive consulting contract that contains non-competition covenants. Our current agreement with David Oakey Designs extends to April 2014. The loss of any of these key persons could have an adverse impact on our business because each has a great deal of knowledge, training and experience in the carpet industry particularly in the areas of sales, marketing, operations, product design and management and could not easily or quickly be replaced.

Our substantial international operations are subject to various political, economic and other uncertainties that could adversely affect our business results, including by restrictive taxation or other government regulation and by foreign currency fluctuations.

We have substantial international operations. In 2012, approximately half of our net sales and a significant portion of our production were outside the United States, primarily in Europe and Asia-Pacific. Our corporate strategy includes the expansion and growth of our international business on a worldwide basis. As a result, our operations are subject to various political, economic and other uncertainties, including risks of restrictive taxation policies, changing political conditions and governmental regulations. We also make a substantial portion of our net sales in currencies other than U.S. dollars (approximately half of 2012 net sales), which subjects us to the risks inherent in currency translations. The scope and volume of our global operations make it impossible to eliminate completely all foreign currency translation risks as an influence on our financial results.

Concerns regarding the European sovereign debt crisis and market perceptions about the instability of the euro, the potential re-introduction of individual currencies within the Eurozone, or the potential dissolution of the euro entirely, could adversely affect our business, results of operations or financial condition.

As a result of the European sovereign debt crisis, concerns persist regarding the debt burden of certain countries using the euro as their currency (the Eurozone) and their ability to meet future financial obligations, the overall stability of the euro and the suitability of the euro as a single currency given the diverse economic and political circumstances in individual Eurozone countries. Despite remedial efforts being taken by the European Commission and others, these concerns have caused instability in the euro and could lead to the re-introduction of individual currencies in one or more Eurozone countries, or, in more extreme circumstances, the possible dissolution of the euro currency entirely. Should the euro dissolve entirely, the legal and contractual consequences for holders of euro-denominated obligations would be determined by laws in effect at such time. These potential developments, or market perceptions concerning these and related issues, could adversely affect the value of our euro-denominated assets and obligations or increase the risks of foreign currency fluctuations or cause the failure of hedging programs intended to reduce those risks. In addition, concerns over the effect of this financial crisis on financial institutions in Europe and globally could have an adverse impact on the capital markets generally, and more specifically on our ability and the ability of our customers, suppliers and lenders to finance our and their respective businesses, to access liquidity at acceptable financing costs, if at all, on the availability of supplies and materials, and on the demand for our products.

Large increases in the cost of petroleum-based raw materials could adversely affect us if we are unable to pass these cost increases through to our customers.

Petroleum-based products comprise the predominant portion of the cost of raw materials that we use in manufacturing. While we attempt to match cost increases with corresponding price increases, continued volatility in the cost of petroleum-based raw materials could adversely affect our financial results if we are unable to pass through such price increases to our customers.

Unanticipated termination or interruption of any of our arrangements with our primary third party suppliers of synthetic fiber could have a material adverse effect on us.

The unanticipated termination or interruption of any of our supply arrangements with our current suppliers of synthetic fiber (nylon), which typically are not pursuant to long-term agreements, could have a material adverse effect on us because we do not have the capability to manufacture our own fiber for use in our carpet products. If any of our supply arrangements with our primary suppliers of synthetic fiber is terminated or interrupted, we likely would incur increased manufacturing costs and experience delays in our manufacturing process (thus resulting in decreased sales and profitability) associated with shifting more of our synthetic fiber purchasing to another synthetic fiber supplier.

We have a significant amount of indebtedness, which could have important negative consequences to us.

Our significant indebtedness could have important negative consequences to us, including:

- making it more difficult for us to satisfy our obligations with respect to such indebtedness;
- increasing our vulnerability to adverse general economic and industry conditions;
- limiting our ability to obtain additional financing to fund capital expenditures, acquisitions or other growth initiatives, and other general corporate requirements;
- requiring us to dedicate a substantial portion of our cash flow from operations to interest and principal payments on our indebtedness, thereby reducing the availability of our cash flow to fund capital expenditures, acquisitions or other growth initiatives, and other general corporate requirements;
- limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- placing us at a competitive disadvantage compared to our less leveraged competitors; and
- limiting our ability to refinance our existing indebtedness as it matures.

As a consequence of our level of indebtedness, a substantial portion of our cash flow from operations must be dedicated to debt service requirements. In addition, the terms of our primary revolving credit facility in the U.S. and the indenture governing our 7 5/8% Senior Notes due 2018 limit our ability and the ability of our subsidiaries to, among other things, incur additional indebtedness, pay dividends or make certain other restricted payments or investments in certain situations, consummate certain asset sales, enter into certain transactions with affiliates, create liens, merge or consolidate with any other person, or sell, assign, transfer, lease, convey or otherwise dispose of all or substantially all of our assets. They also require us to comply with certain other reporting, affirmative and negative covenants and, at times, meet certain financial tests. If we fail to satisfy these tests or comply with these covenants, a default may occur, in which case the lenders could accelerate the debt as well as any other debt to which cross-acceleration or cross-default provisions apply. We cannot assure you that we would be able to renegotiate, refinance or otherwise obtain the necessary funds to satisfy these obligations.

The market price of our common stock has been volatile and the value of your investment may decline.

The market price of our common stock has been volatile in the past and may continue to be volatile going forward. Such volatility may cause precipitous drops in the price of our common stock on the Nasdaq Global Select Market and may cause your investment in our common stock to lose significant value. As a general matter, market price volatility has had a significant effect on the market values of securities issued by many companies for reasons unrelated to their operating performance. We thus cannot predict the market price for our common stock going forward.

Our earnings in a future period could be adversely affected by non-cash adjustments to goodwill, if a future test of goodwill assets indicates a material impairment of those assets.

As prescribed by accounting standards governing goodwill and other intangible assets, we undertake an annual review of the goodwill asset balance reflected in our financial statements. Our review is conducted during the fourth quarter of the year, unless there has been a triggering event prescribed by applicable accounting rules that warrants an earlier interim testing for possible goodwill impairment. In the past, we have had non-cash adjustments for goodwill impairment as a result of such testings ($61.2 million in 2008 and $44.5 million in 2007). A future goodwill impairment test may result in a future non-cash adjustment, which could adversely affect our earnings for any such future period.

Our Rights Agreement could discourage tender offers or other transactions for our stock that could result in shareholders receiving a premium over the market price for our stock.

Our Board of Directors has adopted a Rights Agreement pursuant to which holders of our common stock will be entitled to purchase from us a fraction of a share of our Series B Participating Cumulative Preferred Stock if a third party acquires beneficial ownership of 15% or more of our common stock without our consent. In addition, the holders of our common stock will be entitled to purchase the stock of an Acquiring Person (as defined in the Rights Agreement) at a discount upon the occurrence of triggering events. These provisions of the Rights Agreements could have the effect of discouraging tender offers or other transactions that could result in shareholders receiving a premium over the market price for our common stock.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We maintain our corporate headquarters in Atlanta, Georgia in approximately 20,000 square feet of leased space. The following table lists our principal manufacturing facilities and other material physical locations (some locations are comprised of multiple buildings), all of which we own except as otherwise noted:

Location	**Floor Space (Sq. Ft.)**
Bangkok, Thailand	275,946
Craigavon, N. Ireland(1)	80,986
LaGrange, Georgia	539,545
LaGrange, Georgia(1)	209,337
Minto, Australia(1)	259,356
Scherpenzeel, the Netherlands	245,420
Scherpenzeel, the Netherlands(1)	121,515
West Point, Georgia	250,000
Taicang, China(1)	71,375

(1) Leased.

Until July of 2012, we manufactured carpet at an owned facility in Picton, Australia, but as a result of a fire this facility is no longer operational. We have leased a new facility in Minto, Australia and expect it to begin manufacturing operations in late 2013.

We maintain marketing offices in over 70 locations in over 30 countries and distribution facilities in approximately 40 locations in six countries. Most of our marketing locations and many of our distribution facilities are leased.

We believe that our manufacturing and distribution facilities and our marketing offices, particularly with the rebuilding of a manufacturing facility in Minto, Australia, are sufficient for our present operations. We will continue, however, to consider the desirability of establishing additional facilities and offices in other locations around the world as part of our business strategy to meet expanding global market demands. Substantially all of our owned properties in the United States, Europe and Australia are subject to mortgages, which secure borrowings under our debt instruments.

ITEM 3. LEGAL PROCEEDINGS

We are subject to various legal proceedings in the ordinary course of business, none of which is required to be disclosed under this Item 3.

ITEM 4. MINING SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Prior to March 5, 2012, the Company had two classes of common stock Class A Common Stock and Class B Common Stock. On March 5, 2012, the number of issued and outstanding shares of Class B Common Stock constituted less than 10% of the aggregate number of issued and outstanding shares of the Company s Class A Common Stock and Class B Common Stock, as the cumulative result of varied transactions that caused the conversion of shares of Class B Common Stock into shares of Class A Common Stock. Accordingly, the Class A Common Stock and Class B Common Stock are now, irrevocably from March 5, 2012, a single class of Common Stock in all respects.

Our Common Stock is traded on the Nasdaq Global Select Market under the symbol TILE. As of February 15, 2013, we had 640 holders of record of our Common Stock. We estimate that there are in excess 5,500 beneficial holders of our Common Stock. The following table sets forth, for the periods indicated, the high and low sale prices of the Company s Common Stock on the Nasdaq Global Select Market as well as dividends paid during such periods.

	High	Low	Dividends Per Share
2013			
First Quarter (through February 15, 2013)	$ 18.96	$ 15.90	$ 0.00
2012			
Fourth Quarter	$ 16.37	$ 12.94	$ 0.025
Third Quarter	14.79	11.62	0.025
Second Quarter	14.89	11.14	0.02
First Quarter	14.08	10.76	0.02
2011			
Fourth Quarter	$ 14.38	$ 9.75	$ 0.02
Third Quarter	20.48	11.02	0.02
Second Quarter	20.23	17.16	0.02
First Quarter	18.49	15.20	0.02

Future declaration and payment of dividends is at the discretion of our Board, and depends upon, among other things, our investment policy and opportunities, results of operations, financial condition, cash requirements, future prospects, and other factors that may be considered relevant by our Board at the time of its determination. Such other factors include limitations contained in the agreement for our primary revolving credit facility and in an indenture for our public indebtedness, each of which specify conditions as to when any dividend payments may be made. As such, we may discontinue our dividend payments in the future if our Board determines that a cessation of dividend payments is proper in light of the factors indicated above.

Stock Performance

The following graph and table compare, for the five-year period ended December 30, 2012, the Company s total returns to shareholders (stock price plus dividends, divided by beginning stock price) with that of (i) all companies listed on the Nasdaq Composite Index, and (ii) a self-determined peer group comprised primarily of companies in the commercial interiors industry, assuming an initial investment of $100 in each on December 30, 2007.

	12/30/07	12/28/08	1/3/10	1/2/11	1/1/12	12/30/12
Interface, Inc.	$ 100	$ 32	$ 52	$ 98	$ 73	$ 100
NASDAQ Composite Index	$ 100	$ 58	$ 87	$ 102	$ 102	$ 117
Previous Self-Determined Peer Group (13 Stocks)	$ 100	$ 40	$ 57	$ 79	$ 75	$ 105
New Self-Determined Peer Group (14 Stocks)	$ 100	$ 41	$ 63	$ 86	$ 84	$ 118

Notes to Performance Graph

(1) The lines represent annual index levels derived from compound daily returns that include all dividends.

(2) The indices are re-weighted daily, using the market capitalization on the previous trading day.

(3) If the annual interval, based on the fiscal year-end, is not a trading day, the preceding trading day is used.

(4) The index level was set to $100 as of December 30, 2007 (the last day of fiscal 2007).

(5) The Company s fiscal year ends on the Sunday nearest December 31.

(6) The following companies are included in the New Self-Determined Peer Group depicted above: Acuity Brands, Inc.; Albany International Corp.; Apogee Enterprises, Inc.; Armstrong World Industries, Inc.; BE Aerospace, Inc.; The Dixie Group, Inc.; Herman Miller, Inc.; HNI Corporation (formerly known as Hon Industries, Inc.); Kimball International, Inc.; Knoll, Inc.; Mohawk Industries, Inc.; Steelcase, Inc.; Unifi, Inc.; and USG Corp. The New Self-Determined Peer Group differs from the Previous Self-Determined Peer Group (also included above for comparison) in the following respects: (i) it includes Apogee Enterprises, Inc. and Armstrong World Industries, Inc., and (ii) it no longer includes Actuant Corp.

Securities Authorized for Issuance Under Equity Compensation Plans

See Item 12 of Part III of this Annual Report on Form 10-K.

ITEM 6. SELECTED FINANCIAL DATA

We derived the summary consolidated financial data presented below from our audited consolidated financial statements and the notes thereto for the years indicated. You should read the summary financial data presented below together with Management s Discussion and Analysis of Financial Condition and Results of Operations and the audited consolidated financial statements and notes thereto included within this document. Amounts for all periods presented have been adjusted for discontinued operations.

	Selected Financial Data[1]				
	2012	**2011**	**2010**	**2009**	**2008**
	(in thousands, except per share data and ratios)				
Net sales	$ 932,020	$ 953,045	$ 862,314	$ 765,264	$ 946,816
Cost of sales	614,841	618,303	549,184	499,078	605,897
Operating income[2]	64,648	85,700	93,107	67,611	102,918
Income (loss) from continuing operations[3]	22,899	38,270	10,297	15,777	26,850
Income (loss) from discontinued operations, net of tax[4]	(16,956)	451	(963)	(4,013)	(66,517)
Net income (loss) attributable to Interface, Inc.	5,943	38,721	8,283	10,918	(40,873)
Income (loss) from continuing operations per common share attributable to Interface, Inc.					
Basic	$ 0.35	$ 0.59	$ 0.14	$ 0.24	$ 0.43
Diluted	$ 0.35	$ 0.58	$ 0.14	$ 0.24	$ 0.42
Average Shares Outstanding					
Basic	65,767	65,291	63,794	63,213	63,005
Diluted	65,900	65,486	64,262	63,308	63,276
Cash dividends per common share	$ 0.09	$ 0.08	$ 0.04	$ 0.01	$ 0.12
Property additions	42,428	38,050	31,715	8,753	29,300
Depreciation and amortization	29,175	35,317	27,927	25,189	23,664
Working capital	$ 268,825	$ 271,625	$ 238,937	$ 265,280	$ 240,123
Total assets	789,367	772,272	755,433	727,239	706,035
Total long-term debt	275,000	294,507	294,428	280,184	287,588
Shareholders equity	295,702	281,039	248,872	246,181	217,437
Current ratio[5]	2.7	2.8	2.4	2.9	2.6

(1) In the third quarter of 2012, we sold our Bentley Prince Street business. The balances have been adjusted to reflect the discontinued operations of this business. For further analysis, see Notes to Consolidated Financial Statements Discontinued Operations included in Item 8 of this Report.

(2) The following charges and items are included in our operating income. In 2012, we recorded restructuring and asset impairment charges of $19.4 million as well as expenses related to the Australia fire of $1.7 million. In 2011, we recorded a restructuring and asset impairment charge of $5.8 million. In 2010 we recorded a restructuring charge of $2.9 million. In 2009, we recorded restructuring charges of $6.9 million. Also in 2009, we recorded income from litigation settlements of $5.9 million. In 2008, we recorded a restructuring charge of $10.9 million.

(3) Included in the 2010 income from continuing operations are pre-tax expenses of $44.4 million related to bond retirement. Included in the 2008 loss from continuing operations is tax expense of $13.3 million related to the anticipated repatriation in 2009 of foreign earnings.

(4) Included in loss from discontinued operations, net of tax, are goodwill and other intangible asset impairment charges of $61.2 million in 2008 related to our Bentley Prince Street business which was subsequently sold in 2012. Also included in loss from discontinued operations, net of tax, are charges for write-offs and impairments of other assets of $5.2 million in 2008 related to our former Fabrics business segment which was sold in 2007.

(5) Current ratio is the ratio of current assets to current liabilities. For purposes of computing our current ratio: (a) current assets include assets of businesses held for sale of $60.7 million for 2011, $55.6 million for 2010, $55.3 million for 2009 and $71.5 million for 2008. Current liabilities include liabilities of businesses held for sale of $8.3 million for 2011, $7.9 million for 2010, $2.4 million for 2009 and $7.8 million for 2008.

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

General

Our revenues are derived from sales of floorcovering products, primarily modular carpet (we sold our broadloom carpet operations in August 2012). Our business, as well as the commercial interiors industry in general, is cyclical in nature and is impacted by economic conditions and trends that affect the markets for commercial and institutional business space. The commercial interiors industry, including the market for floorcovering products, is largely driven by reinvestment by corporations into their existing businesses in the form of new fixtures and furnishings for their workplaces. In significant part, the timing and amount of such reinvestments are impacted by the profitability of those corporations. As a result, macroeconomic factors such as employment rates, office vacancy rates, capital spending, productivity and efficiency gains that impact corporate profitability in general, also affect our business.

During the past several years, we have successfully focused more of our marketing and sales efforts on non-corporate office segments to reduce somewhat our exposure to economic cycles that affect the corporate office market segment more adversely, as well as to capture additional market share. Our mix of corporate office versus non-corporate office modular carpet sales in the Americas has shifted over the past several years to 47% and 53%, respectively, for 2012 compared with 64% and 36%, respectively, in 2001. Company-wide, our mix of corporate office versus non-corporate office sales was 61% and 39%, respectively, in 2012. We expect a further shift in the future as we continue to implement our market diversification strategy.

During 2012, we had net sales of $932.0 million, compared with $953.0 million in 2011. Operating income for 2012 was $64.6 million, compared with $85.7 million for 2011. Income from continuing operations for 2012 was $22.9 million, or $0.35 per diluted share, compared with $38.3 million, or $0.58 per diluted share, in 2011. Net income for 2012 was $5.9 million, or $0.09 per diluted share, compared with $38.7 million, or $0.59 per diluted share, in 2011.

Included for our results for 2012 are $19.4 million of restructuring and asset impairment charges and $1.7 million of expenses related to the fire at our Australian manufacturing facility, as discussed below. Also included in our 2012 results is a loss from discontinued operations, net of tax, of $17.0 million related to the now discontinued Bentley Prince Street business segment. Included in our results for 2011 are $5.8 million of restructuring charges. Included in our results for 2010 are bond retirement expenses of $44.4 million related to our repurchases of our 11 3/8% Senior Secured Notes and 9.5% Senior Subordinated Notes, as well as restructuring charges of $2.9 million.

Fire at Australia Facility

In July 2012, a fire occurred at our manufacturing facility in Picton, Australia. The fire caused extensive damage to the facility, as well as disruption to business activity in the region. We have taken steps towards re-adapting our supply chain with product from our facilities in China, Thailand, the U.S. and Europe. While this is being executed with success, there were, as expected, delays in shipments that affected sales following the fire. At this time, it is difficult to quantify the financial impacts of the fire, but we believe it negatively affected net sales by approximately $13-18 million during the balance of 2012. For additional information on the fire, please see the Note entitled Fire at Australian Manufacturing Facility in Item 8 of this Report.

Discontinued Operations

In the third quarter of 2012, we sold our Bentley Prince Street business segment. In accordance with applicable accounting standards, we have reported the results of operations for the former Bentley Prince Street business segment as discontinued operations, where applicable. Consequently, our discussion of sales and other results of operations (except for net income or loss amounts), including percentages derived from or based on such amounts, excludes these discontinued operations unless we indicate otherwise.

Our discontinued operations had net sales of $57.0 million, $104.0 million and $99.5 million in 2012, 2011 and 2010, respectively (these results are included in our statements of operations as part of the Income (loss) from discontinued operations, net of tax). Income (loss) from discontinued operations, inclusive of the loss on disposal as well as costs to sell the business, net of tax, was ($17.0) million in 2012, $0.5 million in 2011 and ($1.0) million in 2010. For additional information on discontinued operations, see the Notes entitled Discontinued Operations and Taxes on Income in Item 8 of this Report.

Restructuring Charges

2012 Restructuring Plan

In the first quarter of 2012, we committed to a new restructuring plan in our continuing efforts to reduce costs across our worldwide operations and more closely align our operations with reduced demand levels in certain markets. The plan primarily consisted of ceasing manufacturing and warehousing operations at our facility in Shelf, England. In connection with this restructuring plan, we incurred a pre-tax restructuring and asset impairment charge in the first quarter of 2012 in an amount of $16.3 million, as well as additional related charges of $0.8 million in the third quarter of 2012 and $2.3 million in the fourth quarter of 2012. These charges are comprised of severance expenses of $8.5 million for a reduction of 145 employees, other related exit costs of $1.6 million, and impairment of assets of approximately $9.4 million. Approximately $10.1 million of the charge will result in cash expenditures, primarily severance expense.

2011 Restructuring Plan

In 2011, we committed to a restructuring plan intended to reduce costs across our worldwide operations and more closely align our operations with reduced demand in certain markets. As a result of this plan, we incurred pre-tax restructuring and asset impairment charges of $5.8 million in 2011. The majority of this charge ($5.0 million) relates to the severance of approximately 90 employees in Europe, Asia and the United States. The remainder of the charge ($0.8 million) relates to contract termination and fixed asset impairment costs. Approximately $5.0 million of this charge will result in cash expenditures, primarily severance expenses. Actions and expense related to this plan were substantially completed by the end of 2011.

2010 Restructuring Plan

In 2010, we adopted a restructuring plan primarily related to workforce reduction in our European modular carpet operations. This reduction was in response to the continued challenging economic climate in that region. Smaller amounts were incurred in connection with restructuring activities in the Americas. A total of approximately 50 employees were affected by this restructuring plan. In connection with this plan, we recorded a pre-tax restructuring charge of $2.9 million. Substantially all of this charge involved cash expenditures, primarily severance expenses. Actions and expenses related to this plan were substantially completed in 2010.

7 5/8% Senior Notes

On December 3, 2010, we completed a private offering of $275 million aggregate principal amount of 7 5/8% Senior Notes due 2018 (the 7 5/8% Senior Notes). Interest on the 7 5/8% Senior Notes is payable semi-annually on June 1 and December 1 (the first payment was on June 1, 2011). We used the net proceeds from the sale of the 7 5/8% Senior Notes (plus cash on hand) in connection with the repurchase of approximately $141.9 million aggregate principal amount of our 11 3/8% Senior Secured Notes and approximately $98.5 million aggregate principal amount of our 9.5% Senior Subordinated Notes, pursuant to a tender offer we conducted in 2010. We incurred $44.4 million of bond retirement expenses in 2010 in connection with these repurchases pursuant to the tender offer.

11 3/8% Senior Secured Notes

On June 5, 2009, we completed a private offering of $150 million aggregate principal amount of 11 3/8% Senior Secured Notes due 2013 (the 11 3/8% Senior Secured Notes). Interest on the 11 3/8% Senior Secured Notes is payable semi-annually on May 1 and November 1 (the first interest payment was on November 1, 2009). The 11 3/8% Senior Secured Notes are guaranteed, jointly and severally, on a senior secured basis by certain of our domestic subsidiaries. The 11 3/8% Senior Secured Notes are secured by a second-priority lien on substantially all of our and certain of our domestic subsidiaries assets that secure our domestic revolving credit facility (discussed below) on a first-priority basis.

Following the sale of our 7 5/8% Senior Notes and the repurchase of $141.9 million aggregate principal amount of our 11 3/8% Senior Secured Notes with the proceeds, $8.1 million aggregate principal amount of our 11 3/8% Senior Secured Notes remain outstanding.

The 11 3/8% Senior Secured Notes were sold at a price of 96.301% of their face value, resulting in $144.5 million of gross proceeds. The $5.5 million original issue discount is being amortized over the life of the notes through interest expense, although substantially all of this discount was accelerated and charged in 2010 as a result of our repurchases in the tender offer we conducted for these notes in connection with the issuance of our 7 5/8% Senior Notes.

Redemption of 9.5% Senior Subordinated Notes due 2014

In the first quarter of 2010, we redeemed $25 million aggregate principal amount of our 9.5% Senior Subordinated Notes (the 9.5% Senior Subordinated Notes) at a price equal to 103.167% of the face value of the notes, plus accrued interest to the redemption date. We incurred $1.1 million of bond retirement expenses in connection with these repurchases. In the fourth quarter of 2010, we repurchased $98.5 million aggregate principal amount of these notes pursuant to the tender offer discussed above in connection with the issuance of the 7 5/8% Senior Notes. Following such redemption and repurchase of our 9.5% Senior Subordinated Notes, $11.5 million aggregate principal amount of our 9.5% Senior Subordinated Notes remained outstanding. In April 2012, we redeemed the balance of the 9.5% Senior Subordinated Notes at a price equal to 100% of the face value of the notes, plus accrued interest to the redemption date.

Analysis of Results of Operations

The following discussion and analyses reflect the factors and trends discussed in the preceding sections.

Our net sales that were denominated in currencies other than the U.S. dollar were approximately 51% in 2012, 54% in 2011, and 55% in 2010. Because we have such substantial international operations, we are impacted, from time to time, by international developments that affect foreign currency transactions. For example, the performance of the euro against the U.S. dollar, for purposes of the translation of European revenues into U.S. dollars, favorably affected our reported results during 2011, when the euro was strengthening relative to the U.S. dollar. During the years 2012 and 2010, the dollar strengthened versus the euro, having the opposite effect on our reported results. The following table presents the amount (in U.S. dollars) by which the exchange rates for converting euros into U.S. dollars have affected our net sales and operating income during the past three years:

	2012	**2011**	**2010**
		(in millions)	
Net sales	$ (23.5)	$ 14.6	$ (14.4)
Operating income	(2.0)	1.4	(2.1)

The following table presents, as a percentage of net sales, certain items included in our Consolidated Statements of Operations during the past three years:

		Fiscal Year	
	2012	**2011**	**2010**
Net sales	100.0%	100.0%	100.0%
Cost of sales	66.0	64.9	63.7
Gross profit on sales	34.0	35.1	36.3
Selling, general and administrative expenses	24.8	25.5	25.2
Restructuring and asset impairment charges	2.1	0.6	0.3
Expenses related to Australia fire	0.2	0.0	0.0
Operating income	6.9	9.0	10.8
Interest/Other expense	2.9	2.8	4.0
Bond retirement expenses	0.0	0.0	5.1
Income from continuing operations before tax	4.1	6.2	1.7
Income tax expense	1.6	2.2	0.5
Income from continuing operations	2.5	4.0	1.2
Discontinued operations, net of tax	(1.8)	0.0	(0.1)
Net income	0.6	4.1	1.1
Net income attributable to Interface, Inc.	0.6	4.1	1.0

Net Sales

Below we provide information regarding our net sales and analyze those results for each of the last three fiscal years. Fiscal years 2012, 2011 and 2010 were 52-week periods. (As a result of the sale of our Bentley Prince Street Segment in 2012, we currently have only one segment for segment reporting purposes.)

	Fiscal Year (in thousands)			Percentage Change	
	2012	**2011**	**2010**	**2012 compared with 2011**	**2011 compared with 2010**
Net Sales	$ 932,020	$ 953,045	$ 862,314	(2.2)%	10.5%

For 2012, net sales decreased $21.0 million (2.2%) versus 2011. On a worldwide basis, the general economic uncertainty has had an impact on buyers of our product, as we experienced declines in almost all market segments with the exception of the residential market. On a geographic basis, we experienced a sales increase in the Americas (up 5.1%), which was offset by decreases in Europe (down 8.1%) and Asia-Pacific (down 13.2%). In the Americas, the increase in sales was due to the continued rebound of the corporate office market (up 7%), as well as increases in the residential (up 23%) and education (up 6%) market segments. The increase in residential was largely as a result of the continuing roll-out of our FLOR stores, which now comprises 17 locations across the United States and one store in Canada. These increases in the Americas were somewhat offset by decreases in the government (down 10%) and healthcare (down 7%) market segments. The weighted average selling price per square yard in the Americas saw an increase of approximately 5% in 2012. In Europe, currency translation was the driving factor behind the 2012 decrease, as we experienced a decline of 8% as reported in U.S. dollars, but in local currency the sales were essentially even with the prior year. All market segments in Europe experienced a decline as reported in U.S. dollars, with corporate office being the most significant (down 6%). On a local currency basis, however, the corporate office segment saw a 2% increase, which was mitigated by smaller decreases in the retail (down 13%) and government (down 7%) market segments. The weighted average selling price per square yard in Europe was down approximately 3% in U.S. dollars, but up approximately 5% in local currency. Due largely to both the fire in our plant in Australia in July of 2012, as well as the lack of government stimulus funds in 2012 versus 2011, we experienced a sales decline in the Asia-Pacific region of 13% versus 2011. While it is difficult to quantify, we believe that the fire at our Australia facility and the related delays in shipments while we worked to stabilize our supply chain led to a reduction of $13-$18 million in net sales for 2012. The most significant decline was in the education market (down 52%) due to the curtailment of government stimulus in the region, particularly in Australia. The decline in Asia-Pacific was also fueled by lower sales in the hospitality (down 44%) and corporate office (down 3%) market segments. The weighted average selling price in the Asia-Pacific region was essentially even compared with 2011. We have begun building a new facility in Australia which we hope to have completed by the fourth quarter of 2013. We believe this new facility, coupled with the stabilization of our supply chain from other facilities, will help improve performance in Asia-Pacific in 2013.

For 2011, net sales increased $90.7 million (10.5%) versus 2010. The weighted average selling price per square yard increased approximately 4% in 2011 versus 2010. On a geographic basis, we experienced increases in net sales in all regions for 2011 versus 2010, with our Americas, Europe and Asia-Pacific regions experiencing sales growth of 9%, 15% and 7%, respectively (Europe experienced 10% sales growth in local currency). The recovery of the corporate office market was the largest factor in this increase in sales, although smaller increases occurred in certain non-office commercial market segments. In the Americas, the corporate office market segment saw an increase of 16% during 2011. Success in certain non-office commercial markets also fueled the sales increase, particularly in the education (up 8%), healthcare (up 14%) and retail (up 6%) market segments. Sales in the residential market segment, helped by the opening of 5 new FLOR stores during the year, showed an improvement of 22% during 2011. These increases were offset somewhat by sales decreases in the government (down 11%) and hospitality (down 39%) market segments. Sales growth in Europe was also due to the strength of the corporate office market segment (up 19% in U.S. dollars, 14% in local currency), as well as success in the government (up 11% in U.S. dollars, 5% in local currency) and education (up 13% in U.S. dollars, 6% in local currency) market segments. These gains were somewhat offset by a decline in the residential market segment (down 47% in U.S. dollars, 50% in local currency) in Europe. As in our other geographic areas, the increased sales in Asia-Pacific were due to the strength of the corporate office market segment (up 13%). Asia-Pacific also saw increases in the healthcare (up 40%) and hospitality (up 26%) market segments. These increases were partially offset by sales decreases in the education (down 15%) and government (down 18%) market segments.

Cost and Expenses

The following table presents our overall cost of sales and selling, general and administrative expenses during the past three years:

	Fiscal Year			Percentage Change	
Cost and Expenses	**2012**	**2011** *(in thousands)*	**2010**	**2012 compared with 2011**	**2011 compared with 2010**
Cost of Sales	$ 614,841	$ 618,303	$ 549,184	(0.5)%	12.6%
Selling, General and Administrative Expenses	231,358	243,287	217,080	(4.9)%	12.1%
Total	$ 846,199	$ 861,590	$ 766,264	(1.8)%	12.4%

For 2012, our cost of sales decreased $3.5 million (0.5%) versus 2011. Fluctuations in currency exchange rates resulted in approximately $10 million of decrease in cost of sales, so absent currency translation effects, there was an increase in the cost of sales in 2012 versus 2011. The increase absent currency translation effects is primarily attributable to (1) a 3-4% increase in raw material prices in 2012 versus 2011, (2) lower absorption of fixed manufacturing costs associated with lower production volumes in 2012 versus 2011, and (3) supply chain disruption in the second half of 2012 as a result of the fire at our facility in Picton, Australia. Due to these factors, we saw in increase in cost of sales as a percentage of sales to 66.0% in 2012 versus 64.9% in 2011. We did see improvement in gross margin in the fourth quarter of 2012 versus the comparable period in 2011 due to higher absorption of fixed costs due to higher production volumes, as well as the beginning of realization of savings from our 2012 restructuring plans. However, this quarterly improvement was not substantial enough to counteract the above factors in the earlier parts of the year.

For 2011, our cost of sales increased $69.1 million (12.6%) versus 2010. Fluctuations in currency exchange rates accounted for approximately $17 million (approximately 3%) of the increase. The primary components of this increase in cost of sales were the increases in raw materials costs (approximately $46 million) and labor costs (approximately $7 million) associated with higher production volumes, particularly in the first six months of 2011, compared with 2010. In addition, our raw materials costs during 2011 were approximately 7-9% higher than raw materials costs in the prior year. As a percentage of net sales, cost of sales increased to 64.9% for 2011, versus 63.7% in 2010. This percentage increase is primarily due to the significant increase in raw materials costs we experienced during 2011. Reduced absorption of fixed manufacturing costs due to lower production volumes during the fourth quarter of 2011 also negatively impacted gross profit margins as well.

For 2012, our selling, general and administrative expenses decreased $11.9 million (4.9%) versus 2011. Fluctuations in currency exchange rates accounted for approximately $4 million (1.5%) of the decrease. The largest component of the change in selling, general and administrative expense was a decrease in administrative costs of approximately $14 million, which is due primarily to lower stock compensation expense of $6 million during the first six months of 2012, particularly in the Americas, as a result of performance goals not being obtained to the same degree as in 2011. There also was a decrease in administrative expenses due to the significant restructuring actions which took place in 2011 and 2012, particularly in our European operations. We also experienced a decrease of $4 million in marketing expense, particularly in the Americas, due to lower catalog circulation in our FLOR business (approximately $1 million), as well as reduced marketing programs as we evaluate the cost effectiveness of our marketing platform in light of market requirements. These decreases were offset somewhat by increased selling costs of $7 million, primarily in the Americas, due to both the FLOR store rollout (approximately $2 million) as well as sales personnel additions in the Americas in response to positive market conditions in that region, and increased selling costs due to increased sales in the Americas (approximately $3 million increase.) Due to the above factors, as a percentage of net sales, selling, general and administrative costs declined to 24.8% in 2012 versus 25.5% in 2011.

For 2011, our selling, general and administrative expenses increased $26.2 million (12.1%) versus 2010. Fluctuations in currency exchange rates accounted for approximately $7 million (3%) of the increase. The primary components of this increase in selling, general and administrative expenses were (1) a $14.1 million increase in selling expense, commensurate with the increase in sales as well as selected investments made in our consumer market and diversification strategies, (2) an $11.1 million increase in overall administrative costs due, in part, to increases in non-cash incentive based pay during 2011, particularly in the first six months of the year. Due to these increases, as a percentage of net sales, selling, general and administrative expenses increased to 25.5% for 2011, versus 25.2% for 2010.

Interest Expense

For 2012 interest expense decreased $1.3 million versus 2011. This decrease was primarily due to the redemption of the remaining $11.5 million our 9.5% Senior Subordinated Notes due 2014 in April of 2012.

For 2011 interest expense decreased $6.9 million versus 2010. This decrease was due to the issuance of our 7 5/8% Senior Notes in the fourth quarter of 2010, the proceeds of which we used to complete the repurchase of substantially all of our 11 3/8% Senior Secured Notes and our outstanding 9.5% Senior Subordinated Notes pursuant to the tender offer discussed above. Our use of the proceeds from our 7 5/8% Senior Notes to retire higher interest debt led to a significant reduction in our interest expense, as compared to 2010.

Tax

Our effective tax rate in 2012 was 39.9%, compared with an effective rate of 35.0% in 2011. This increase in effective rate was primarily attributable to (1) nondeductible business expenses associated with the fire at the Australia plant, and (2) a nondeductible reserve on capital assets associated with our 2012 restructuring plan. In addition, there were decreases in the effective rate attributable to the cash surrender value of life insurance policies and tax effects of undistributed earnings from foreign subsidiaries not deemed to be indefinitely reinvested, which were offset by increases in the effective rate for foreign and U.S tax effects attributable to foreign operations. For additional information on taxes and a reconciliation of effective tax rates to statutory tax rates, see the Note entitled Taxes on Income in Item 8 of this Report.

Our effective tax rate in 2011 was 35.0%, compared with an effective rate of 30.9% in 2010. This increase in effective rate was primarily attributable to (1) a decrease in the cash surrender value of life insurance policies associated with the funding of our nonqualified savings plan and salary continuation plan resulting in nondeductible losses in 2011 as compared with an increase in 2010, which resulted in nontaxable gains, (2) a decrease in state tax benefits due to less state net operating losses in 2011 as compared with 2010, and (3) less of a decrease in unrecognized tax benefits in 2011 as compared with 2010. The increase in effective rate was partially offset by a decrease in valuation allowances related to state net operating loss carryforwards and a decrease in the U.S. tax effects attributable to foreign operations related to Subpart F income. For additional information on taxes and a reconciliation of effective tax rates to statutory tax rates, see the Note entitled Taxes on Income in Item 8 of this Report.

Liquidity and Capital Resources

General

In our business, we require cash and other liquid assets primarily to purchase raw materials and to pay other manufacturing costs, in addition to funding normal course selling, general and administrative expenses, anticipated capital expenditures, interest expense and potential special projects. We generate our cash and other liquidity requirements primarily from our operations and from borrowings or letters of credit under our domestic revolving credit facility with a banking syndicate. We believe that we will be able to continue to enhance the generation of free cash flow through the following initiatives:

- Improving our inventory turns by continuing to implement a made-to-order model throughout our organization;

- Reducing our average days sales outstanding through improved credit and collection practices; and

- Limiting the amount of our capital expenditures generally to those projects that have a short-term payback period.

Historically, we use more cash in the first half of the fiscal year, as we fund insurance premiums, tax payments, incentive compensation and inventory build-up in preparation for the holiday/vacation season of our international operations.

In addition, we have a high contribution margin business with low capital expenditure requirements. Contribution margin represents variable gross profit margin less the variable component of selling, general and administrative expenses, and for us is an indicator of profit on incremental sales after the fixed components of cost of goods sold and selling, general and administrative expenses have been recovered. While contribution margin should not be construed as a substitute for gross margin, which is determined in accordance with GAAP, it is included herein to provide additional information with respect to our potential for profitability. In addition, we believe that investors find contribution margin to be a useful tool for measuring our profitability on an operating basis.

At December 30, 2012, we had $90.5 million in cash. Approximately $50.3 million of this cash was located in the Unites States, and the remaining $40.2 million was located at our international locations. Our position is that the cash located outside of the United States is permanently reinvested in the respective jurisdictions (except as identified below). We believe that our strategic plans and business needs support the status of our cash in foreign locations (particularly as we build our new facility in Minto, Australia and review other international investment opportunities). Of the $40.2 million in cash in foreign jurisdictions, approximately $9.2 million represents earnings which we have determined are not permanently reinvested, and as such we have provided for U.S. federal and state income taxes on these amounts in accordance with applicable accounting standards.

As of December 30, 2012, we had no borrowings and $3.9 million in letters of credit outstanding under our domestic revolving credit facility, and no borrowings outstanding under our European credit facility. As of December 30, 2012, we could have incurred $62.8 million of additional borrowings under our domestic revolving credit facility and 20.0 million (approximately $26.5 million) of additional borrowings under our European credit facility. In addition, we could have incurred the equivalent of $18.9 million of borrowings under our other credit facilities in place at other non-U.S. subsidiaries.

We have approximately $65.1 million in contractual cash obligations due by the end of fiscal year 2013, which includes, among other things, pension cash contributions, interest payments on our debt and capital expenditure commitments. Based on current interest rate and debt levels, we expect our aggregate interest expense for 2013 to be between $23 million and $26 million. We estimate aggregate capital expenditures in 2013 to be between $30 million and $40 million, although we are not committed to these amounts.

On December 3, 2010, we completed a private offering of $275 million aggregate principal amount of 7 5/8% Senior Notes. Interest on the 7 5/8% Senior Notes is payable semi-annually on June 1 and December 1 (the first payment was made on June 1, 2011). We used the net proceeds from the sale of the 7 5/8% Senior Notes (plus cash on hand) in connection with the repurchase of approximately $141.9 million aggregate principal amount of our 11 3/8% Senior Secured Notes and approximately $98.5 million aggregate principal amount of the 9.5% Senior Subordinated Notes, pursuant to a tender offer we conducted.

We also have $8.1 million aggregate principal amount outstanding of our 11 3/8% Senior Secured Notes.

It is important for you to consider that we have a significant amount of indebtedness. Our outstanding $8.1 million of 11 3/8% Senior Secured Notes mature in November 2013, our domestic revolving credit facility matures in June 2016, and our outstanding $275 million of 7 5/8% Senior Notes mature in 2018. We cannot assure you that we will be able to renegotiate or refinance any of our debt on commercially reasonable terms, or at all. If we are unable to refinance our debt or obtain new financing, we would have to consider other options, such as selling assets to meet our debt service obligations and other liquidity needs, or using cash, if available, that would have been used for other business purposes.

Domestic Revolving Credit Facility

We have a domestic revolving credit facility that provides for a maximum aggregate amount of loans and letters of credit of up to $100 million (with the option to increase it to a maximum of $150 million upon the satisfaction of certain conditions) at any one time, subject to the borrowing base described below. The key features of the domestic revolving credit facility are as follows:

The revolving credit facility currently matures on June 24, 2016;

The revolving credit facility includes a domestic U.S. dollar syndicated loan and letter of credit facility made available to Interface, Inc. up to the lesser of (1) $100 million, or (2) a borrowing base equal to the sum of specified percentages of eligible accounts receivable and inventory in the United States (the percentages and eligibility requirements for the borrowing base are specified in the credit facility), less certain reserves;

Advances under the facility are secured by a first-priority lien on substantially all of Interface, Inc. s assets and the assets of each of its material domestic subsidiaries, which have guaranteed the revolving credit facility; and

The revolving credit facility contains a financial covenant (a fixed charge coverage ratio test) that becomes effective in the event that our excess borrowing availability falls below 12.5% of the aggregate loan commitments of the lenders. In such event, we must comply with the financial covenant for a period commencing on the last day of the fiscal quarter immediately preceding such event (unless such event occurs on the last day of a fiscal quarter, in which case the compliance period commences on such date) and ending on the last day of the fiscal quarter immediately following the fiscal quarter in which such event occurred.

The revolving credit facility also includes various reporting, affirmative and negative covenants, and other provisions that restrict our ability to take certain actions, including provisions that restrict our ability to repay our long-term indebtedness unless we meet a specified minimum excess availability test.

Interest Rates and Fees. Interest on base rate loans is charged at varying rates computed by applying a margin ranging from 0.75% to 1.25% over the applicable base interest rate (which is defined as the greatest of the prime rate, a specified federal funds rate plus 0.50%, or the one-month LIBOR rate), depending on our average excess borrowing availability during the most recently completed fiscal quarter. Interest on LIBOR-based loans and fees for letters of credit are charged at varying rates computed by applying a margin ranging from 1.75% to 2.25% over the applicable LIBOR rate, depending on our average excess borrowing availability during the most recently completed fiscal quarter. In addition, we pay an unused line fee of 0.375% per annum on the facility.

Prepayments. The revolving credit facility requires prepayment from the proceeds of certain asset sales.

Covenants. The revolving credit facility also limits our ability, among other things, to:

- repay our other indebtedness prior to maturity unless we meet a specified minimum excess availability test;
- incur indebtedness or contingent obligations;
- make acquisitions of or investments in businesses (in excess of certain specified amounts);
- sell or dispose of assets (in excess of certain specified amounts);
- create or incur liens on assets; and
- enter into sale and leaseback transactions.

We are presently in compliance with all covenants under the revolving credit facility and anticipate that we will remain in compliance with the covenants for the foreseeable future.

Events of Default. If we breach or fail to perform any of the affirmative or negative covenants under the revolving credit facility, or if other specified events occur (such as a bankruptcy or similar event or a change of control of Interface, Inc. or certain subsidiaries, or if we breach or fail to perform any covenant or agreement contained in any instrument relating to any of our other indebtedness exceeding $15 million), after giving effect to any applicable notice and right to cure provisions, an event of default will exist. If an event of default exists and is continuing, the lenders agent may, and upon the written request of a specified percentage of the lender group, shall:

- declare all commitments of the lenders under the facility terminated;
- declare all amounts outstanding or accrued thereunder immediately due and payable; and
- exercise other rights and remedies available to them under the agreement and applicable law.

Collateral. The facility is secured by substantially all of the assets of Interface, Inc. and its domestic subsidiaries (subject to exceptions for certain immaterial subsidiaries), including all of the stock of our domestic subsidiaries and up to 65% of the stock of our first-tier material foreign subsidiaries. If an event of default occurs under the revolving credit facility, the lenders collateral agent may, upon the request of a specified percentage of lenders, exercise remedies with respect to the collateral, including, in some instances, foreclosing mortgages on real estate assets, taking possession of or selling personal property assets, collecting accounts receivables, or exercising proxies to take control of the pledged stock of domestic and first-tier material foreign subsidiaries.

Foreign Credit Facilities

Our European subsidiary Interface Europe B.V. and certain of Interface Europe B.V. s subsidiaries have a Credit Agreement with The Royal Bank of Scotland (as successor to ABN AMRO Bank N.V.) (RBS). Under the Credit Agreement, RBS provides a credit facility, until further notice, for borrowings and bank guarantees of up to 20 million.

Interest on borrowings under the facility is charged at varying rates computed by applying a margin of 1% over RBS s euro base rate (consisting of the leading refinancing rate as determined from time to time by the European Central Bank plus a debit interest surcharge), which base rate is subject to a minimum of 3.5% per annum. Fees on bank guarantees and documentary letters of credit are charged at a rate of 1% per annum or part thereof on the maximum amount and for the maximum duration of each guarantee or documentary letter of credit issued. A facility fee of 0.5% per annum is payable with respect to the facility amount. The facility is secured by liens on certain real property, personal property and other assets of our principal European subsidiaries. The facility also includes certain financial covenants (which require the borrowers and their subsidiaries to maintain a minimum interest coverage ratio, total debt/EBITDA ratio and tangible net worth/total assets) and affirmative and negative covenants, and other provisions that restrict the borrowers ability (and the ability of certain of the borrowers subsidiaries) to take certain actions. As of December 30, 2012, there were no borrowings outstanding under this facility.

Some of our other non-U.S. subsidiaries have an aggregate of the equivalent of $18.9 million of lines of credit available. As of December 30, 2012, there were no borrowings outstanding under these lines of credit.

We are presently in compliance with all covenants under these foreign credit facilities and anticipate that we will remain in compliance with the covenants for the foreseeable future.

Senior and Senior Subordinated Notes

As of December 30, 2012, we had outstanding $275 million of our 7 5/8% Senior Notes and $8.1 million of our 11 3/8% Senior Secured Notes. The indentures governing these notes, on a collective basis, contain covenants that limit or restrict our ability to:

- incur additional indebtedness;
- make dividend payments or other restricted payments;
- create liens on our assets;
- sell our assets;
- sell securities of our subsidiaries;
- enter into transactions with shareholders and affiliates; and
- enter into mergers, consolidations or sales of all or substantially all of our assets.

In addition, the indentures governing each series of notes contains a covenant that requires us to make an offer to purchase the outstanding notes under such indenture in the event of a change of control of Interface, Inc. (as defined in each respective indenture).

Each series of notes is guaranteed, fully, unconditionally, and jointly and severally, on an unsecured basis by each of our material U.S. subsidiaries. In addition, the 11 3/8% Senior Secured Notes (but not the 7 5/8% Senior Notes) are secured by a second-priority lien on substantially all of our and certain of our domestic subsidiaries assets that secure our domestic revolving credit facility (discussed above) on a first-priority basis.

28

If we breach or fail to perform any of the affirmative or negative covenants under one of these indentures, or if other specified events occur (such as a bankruptcy or similar event), after giving effect to any applicable notice and right to cure provisions, an event of default will exist. An event of default also will exist under the 7 5/8% Senior Notes indenture if we breach or fail to perform any covenant or agreement contained in any other instrument (including without limitation any other indenture) relating to any of our indebtedness exceeding $20 million and such default or failure results in the indebtedness becoming due and payable. If an event of default exists and is continuing, the trustee of the notes (or the holders of at least 25% of the principal amount of such notes) may declare the principal amount of the notes and accrued interest thereon immediately due and payable (except in the case of bankruptcy, in which case such amounts are immediately due and payable even in the absence of such a declaration). Also, the collateral agent for the 11 3/8% Senior Secured Notes may (subject to the rights of the first priority lien holders under the domestic revolving credit facility) exercise remedies with respect to the collateral securing those notes.

Analysis of Cash Flows

Our primary sources of cash during 2012 were: (1) $32.2 million of net proceeds from the sale of our Bentley Prince Street business segment; (2) $20.0 million as a result of reduction of accounts receivable; and (3) $20.7 million of proceeds from the insurance company with regard to the fire at our Australian facility. Our primary uses of cash during 2012 were: (1) $42.4 million of capital expenditures; (2) an increase of prepaid expenses and other current assets of $11.9 million, primarily related to the insurance receivable for our fire claim in Australia; and (3) $11.5 million for the redemption of the remainder of our 9.5% Senior Subordinated Notes.

Our primary sources of cash during 2011 were: (1) $2.7 million of cash received as a result of exercises of employee stock options; and (2) $1.4 million received due to a reduction of prepaid expenses. Our primary uses of cash during 2011 were: (1) $38.1 million for capital expenditures; (2) $31.6 million due to increased inventory levels; and (3) $17.6 million due to decreases in accounts payable and accruals.

Our primary sources of cash during 2010 were: (1) $275.0 million of gross proceeds from the issuance of our 7 5/8% Senior Notes; (2) $28.2 million due to an increase of accounts payable and accrued expenses; and (3) $3.1 million from the exercise of employee stock options. Our primary uses of cash during 2010 were: (1) $280.0 million used to repurchase a portion of our 11 3/8% Senior Secured Notes and former 9.5% Senior Subordinated Notes; (2) $36.4 million for premiums paid in connection with the repurchase of these senior and senior subordinated notes; (3) $31.7 million for capital expenditures; and (4) $23.1 million due to an increase in inventory.

We believe that our liquidity position will provide sufficient funds to meet our current commitments and other cash requirements for the foreseeable future.

Funding Obligations

We have various contractual obligations that we must fund as part of our normal operations. The following table discloses aggregate information about our contractual obligations (including the remaining contractual obligations related to our discontinued operations) and the periods in which payments are due. The amounts and time periods are measured from December 30, 2012.

	Payments Due by Period				
	Total Payments Due	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
			(in thousands)		
Long-Term Debt Obligations	$ 283,143	$ 8,143	$ 0	$ 0	$ 275,000
Operating Lease Obligations(1)	72,799	21,655	28,665	11,279	11,200
Expected Interest Payments(2)	124,838	21,741	41,938	41,938	19,221
Unconditional Purchase Obligations(3)	2,789	2,723	56	10	0
Pension Cash Obligations(4)	118,686	10,850	22,181	23,265	62,390
Total Contractual Cash Obligations(5)	$ 602,255	$ 65,112	$ 92,840	$ 76,492	$ 367,811

(1) Our capital lease obligations are insignificant.

(2) Expected interest payments to be made in future periods reflect anticipated interest payments related to the $275.0 million of our 7 5/8% Senior Notes, and the $8.1 million of outstanding 11 3/8% Senior Secured Notes. We have also assumed in the presentation above that these notes will remain outstanding until maturity. We have excluded from the presentation interest payments and fees related to our revolving credit facilities (discussed above), because of the variability and timing of advances and repayments thereunder.

(3) Unconditional purchase obligations do not include unconditional purchase obligations that are included as liabilities in our Consolidated Balance Sheet. Our capital expenditure commitments are not significant.

(4) We have two foreign defined benefit plans and a domestic salary continuation plan. We have presented above the estimated cash obligations that will be paid under these plans over the next ten years. Such amounts are based on several estimates and assumptions and could differ materially should the underlying estimates and assumptions change. Our domestic salary continuation plan is an unfunded plan, and we do not currently have any commitments to make contributions to this plan. However, we do use insurance instruments to hedge our exposure under the salary continuation plan. Contributions to our other employee benefit plans are at our discretion.

(5) The above table does not reflect unrecognized tax benefits of $25.2 million, the timing of which payments are uncertain. See the Note entitled Taxes on Income in Item 8 of this Report for further information.

Critical Accounting Policies

The policies discussed below are considered by management to be critical to an understanding of our consolidated financial statements because their application places the most significant demands on management s judgment, with financial reporting results relying on estimations about the effects of matters that are inherently uncertain. Specific risks for these critical accounting policies are described in the following paragraphs. For all of these policies, management cautions that future events may not develop as forecasted, and the best estimates routinely require adjustment.

Revenue Recognition. Revenue is recognized when the following criteria are met: persuasive evidence of an agreement exists, delivery has occurred or services have been rendered, price to the buyer is fixed and determinable, and collectability is reasonably assured. Delivery is not considered to have occurred until the customer takes title and assumes the risks and rewards of ownership, which is generally on the date of shipment. Provisions for discounts, sales returns and allowances are estimated using historical experience, current economic trends, and the company s quality performance. The related provision is recorded as a reduction of sales and cost of sales in the same period that the revenue is recognized. Material differences may result in the amount and timing of net sales for any period if management makes different judgments or uses different estimates.

Shipping and handling fees billed to customers are classified in net sales in the consolidated statements of operations. Shipping and handling costs incurred are classified in cost of sales in the consolidated statements of operations.

Impairment of Long-Lived Assets. Long-lived assets are reviewed for impairment at the asset group level whenever events or changes in circumstances indicate that the carrying value may not be recoverable. If the sum of the expected future undiscounted cash flow is less than the carrying amount of the asset, an impairment is indicated. A loss is then recognized for the difference, if any, between the fair value of the asset (as estimated by management using its best judgment) and the carrying value of the asset. If actual market value is less favorable than that estimated by management, additional write-downs may be required.

Deferred Income Tax Assets and Liabilities. The carrying values of deferred income tax assets and liabilities reflect the application of our income tax accounting policies in accordance with applicable accounting standards, and are based on management s assumptions and estimates regarding future operating results and levels of taxable income, as well as management s judgment regarding the interpretation of the provisions of applicable accounting standards. The carrying values of liabilities for income taxes currently payable are based on management s interpretations of applicable tax laws, and incorporate management s assumptions and judgments regarding the use of tax planning strategies in various taxing jurisdictions. The use of different estimates, assumptions and judgments in connection with accounting for income taxes may result in materially different carrying values of income tax assets and liabilities and results of operations.

We evaluate the recoverability of these deferred tax assets by assessing the adequacy of future expected taxable income from all sources, including reversal of taxable temporary differences, forecasted operating earnings and available tax planning strategies. These sources of income inherently rely heavily on estimates. We use our historical experience and our short and long-term business forecasts to provide insight. Further, our global business portfolio gives us the opportunity to employ various prudent and feasible tax planning strategies to facilitate the recoverability of future deductions. To the extent we do not consider it more likely than not that a deferred tax asset will be recovered, a valuation allowance is established. As of December 30, 2012, and January 1, 2012, we had approximately $128.2 million and $96.2 million of U.S. federal net operating loss carryforwards, respectively. In addition, as of December 30, 2012, and January 1, 2012, we had state net operating loss carryforwards of $187.0 million and $128.0 million, respectively. As of December 30, 2012, and January 1, 2012, we had approximately $3.5 million and $1.5 million of foreign net operating loss carryforwards, respectively. Certain of these carryforwards are reserved with a valuation allowance because, based on the available evidence, we believe it is more likely than not that we would not be able to utilize those deferred tax assets in the future. The remaining year-end 2012 amounts are expected to be fully recoverable within the applicable statutory expiration periods. If the actual amounts of taxable income differ from our estimates, the amount of our valuation allowance could be materially impacted

Goodwill. Pursuant to applicable accounting standards, we test goodwill for impairment at least annually using a two step approach. In the first step of this approach, we prepare valuations of reporting units, using both a market comparable approach and an income approach, and those valuations are compared with the respective book values of the reporting units to determine whether any goodwill impairment exists. In preparing the valuations, past, present and expected future performance is considered. If impairment is indicated in this first step of the test, a step two valuation approach is performed. The step two valuation approach compares the implied fair value of goodwill to the book value of goodwill. The implied fair value of goodwill is determined by allocating the estimated fair value of the reporting unit to the assets and liabilities of the reporting unit, including both recognized and unrecognized intangible assets, in the same manner as goodwill is determined in a business combination under applicable accounting standards. After completion of this step two test, a loss is recognized for the difference, if any, between the fair value of the goodwill associated with the reporting unit and the book value of that goodwill. If the actual fair value of the goodwill is determined to be less than that estimated, an additional write-down may be required.

During the fourth quarters of 2012, 2011 and 2010, we performed the annual goodwill impairment test. We perform this test at the reporting unit level. For our reporting units which carried a goodwill balance as of December 30, 2012, no impairment of goodwill was indicated. As of December 30, 2012, if our estimates of the fair value of our reporting units were 10% lower, we believe no additional goodwill impairment would have existed.

Inventories. We determine the value of inventories using the lower of cost or market. We write down inventories for the difference between the carrying value of the inventories and their net realizable value. If actual market conditions are less favorable than those projected by management, additional write-downs may be required.

We estimate our reserves for inventory obsolescence by continuously examining our inventories to determine if there are indicators that carrying values exceed net realizable values. Experience has shown that significant indicators that could require the need for additional inventory write-downs are the age of the inventory, the length of its product life cycles, anticipated demand for our products and current economic conditions. While we believe that adequate write-downs for inventory obsolescence have been made in the consolidated financial statements, consumer tastes and preferences will continue to change and we could experience additional inventory write-downs in the future. Our inventory reserve on December 30, 2012, and January 1, 2012, was $12.9 million and $10.4 million, respectively. To the extent that actual obsolescence of our inventory differs from our estimate by 10%, our 2012 net income would be higher or lower by approximately $1.0 million, on an after-tax basis.

Pension Benefits. Net pension expense recorded is based on, among other things, assumptions about the discount rate, estimated return on plan assets and salary increases. While management believes these assumptions are reasonable, changes in these and other factors and differences between actual and assumed changes in the present value of liabilities or assets of our plans above certain thresholds could cause net annual expense to increase or decrease materially from year to year. The actuarial assumptions used in our salary continuation plan and our foreign defined benefit plans reporting are reviewed periodically and compared with external benchmarks to ensure that they appropriately account for our future pension benefit obligation. The expected long-term rate of return on plan assets assumption is based on weighted average expected returns for each asset class. Expected returns reflect a combination of historical performance analysis and the forward-looking views of the financial markets, and include input from actuaries, investment service firms and investment managers. The table below represents the changes to the projected benefit obligation as a result of changes in discount rates assumptions:

Foreign Defined Benefit Plans	Increase (Decrease) in Projected Benefit Obligation (in millions)	
1% increase in actuarial assumption for discount rate	$	(43.1)
1% decrease in actuarial assumption for discount rate	$	49.6

Domestic Salary Continuation Plan	Increase (Decrease) in Projected Benefit Obligation (in millions)	
1% increase in actuarial assumption for discount rate	$	(2.7)
1% decrease in actuarial assumption for discount rate	$	3.3

Environmental Remediation. We provide for remediation costs and penalties when the responsibility to remediate is probable and the amount of associated costs is reasonably determinable. Remediation liabilities are accrued based on estimates of known environmental exposures and are discounted in certain instances. We regularly monitor the progress of environmental remediation. Should studies indicate that the cost of remediation is to be more than previously estimated, an additional accrual would be recorded in the period in which such determination is made. As of December 30, 2012, and January 1, 2012, no significant amounts were provided for remediation liabilities.

Allowances for Doubtful Accounts. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of customers to make required payments. Estimating this amount requires us to analyze the financial strengths of our customers. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. By its nature, such an estimate is highly subjective, and it is possible that the amount of accounts receivable that we are unable to collect may be different than the amount initially estimated. Our allowance for doubtful accounts on December 30, 2012, and January 1, 2012, was $8.8 million and $8.9 million, respectively. To the extent the actual collectability of our accounts receivable differs from our estimates by 10%, our 2012 net income would be higher or lower by approximately $0.5 million, on an after-tax basis, depending on whether the actual collectability was better or worse, respectively, than the estimated allowance.

Product Warranties. We typically provide limited warranties with respect to certain attributes of our carpet products (for example, warranties regarding excessive surface wear, edge ravel and static electricity) for periods ranging from ten to twenty years, depending on the particular carpet product and the environment in which the product is to be installed. We typically warrant that any services performed will be free from defects in workmanship for a period of one year following completion. In the event of a breach of warranty, the remedy typically is limited to repair of the problem or replacement of the affected product. We record a provision related to warranty costs based on historical experience and periodically adjust these provisions to reflect changes in actual experience. Our warranty reserve on December 30, 2012, and January 1, 2012, was $1.2 million and $0.9 million, respectively. Actual warranty expense incurred could vary significantly from amounts that we estimate. To the extent the actual warranty expense differs from our estimates by 10%, our 2012 net income would be higher or lower by approximately $0.1 million, on an after-tax basis, depending on whether the actual expense is lower or higher, respectively, than the estimated provision.

Off-Balance Sheet Arrangements

We are not a party to any material off-balance sheet arrangements.

Recent Accounting Pronouncements

In September 2011, the Financial Accounting Standards Board (FASB) issued an accounting standard regarding the performance of a company s annual goodwill impairment evaluation. This standard allows companies to assess qualitative factors to determine if it is more likely than not that goodwill might be impaired and whether it is necessary to perform the two-step goodwill impairment test. This standard is effective for fiscal years beginning after December 31, 2011. The adoption of this standard did not have any significant impact on our consolidated financial statements.

In June 2011, the FASB amended an accounting standard regarding the presentation of comprehensive income. This amendment will require companies to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. It eliminates the option to present components of other comprehensive income as part of the statement of changes in shareholders equity. The amended guidance, which must be applied retroactively, was to be effective for interim and annual periods ending after December 31, 2012, with earlier adoption permitted. In December of 2011, the FASB issued an amendment to this statement which defers the requirements of this standard. As this amendment only effects presentation, there is not expected to be any impact on the Company s consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK
Market Risk

As a result of the scope of our global operations, we are exposed to an element of market risk from changes in interest rates and foreign currency exchange rates. Our results of operations and financial condition could be impacted by this risk. We manage our exposure to market risk through our regular operating and financial activities and, to the extent we deem appropriate, through the use of derivative financial instruments.

We employ derivative financial instruments as risk management tools and not for speculative or trading purposes. We monitor the use of derivative financial instruments through objective measurable systems, well-defined market and credit risk limits, and timely reports to senior management according to prescribed guidelines. We have established strict counter-party credit guidelines and enter into transactions only with financial institutions with a rating of investment grade or better. As a result, we consider the risk of counter-party default to be minimal.

Interest Rate Market Risk Exposure

Changes in interest rates affect the interest paid on certain of our debt. To mitigate the impact of fluctuations in interest rates, our management has developed and implemented a policy to maintain the percentage of fixed and variable rate debt within certain parameters. In the past, we have maintained a fixed/variable rate mix within these parameters either by borrowing on a fixed rate basis or entering into interest rate swap transactions. In the interest rate swaps, we agree to exchange, at specified levels, the difference between fixed and variable interest amounts calculated by reference to an agreed-upon notional principal linked to LIBOR. As of December 30, 2012, and January 1, 2012, no such interest rate swaps were in place.

Foreign Currency Exchange Market Risk Exposure

A significant portion of our operations consists of manufacturing and sales activities in foreign jurisdictions. We manufacture our products in the United States, Northern Ireland, the Netherlands, China and Thailand, and sell our products in more than 100 countries. (In 2012, we ceased manufacturing operations at our facility in England. In addition, manufacturing in Australia has been suspended temporarily as we rebuild following a fire.) As a result, our financial results could be significantly affected by factors such as changes in foreign currency exchange rates or weak economic conditions in the foreign markets in which we distribute our products. Our operating results are exposed to changes in exchange rates between the U.S. dollar and many other currencies, including the euro, British pound sterling, Canadian dollar, Australian dollar, Thai baht and Japanese yen. When the U.S. dollar strengthens against a foreign currency, the value of anticipated sales in those currencies decreases, and vice versa. Additionally, to the extent our foreign operations with functional currencies other than the U.S. dollar transact business in countries other than the United States, exchange rate changes between two foreign currencies could ultimately impact us. Finally, because we report in U.S. dollars on a consolidated basis, foreign currency exchange fluctuations could have a translation impact on our financial position.

At December 30, 2012, we recognized an $8.5 million increase in our foreign currency translation adjustment account compared with January 1, 2012, because of the weakening of the U.S. dollar against certain foreign currencies during 2012.

Sensitivity Analysis

For purposes of specific risk analysis, we use sensitivity analysis to measure the impact that market risk may have on the fair values of our market-sensitive instruments.

To perform sensitivity analysis, we assess the risk of loss in fair values associated with the impact of hypothetical changes in interest rates and foreign currency exchange rates on market-sensitive instruments. The market value of instruments affected by interest rate and foreign currency exchange rate risk is computed based on the present value of future cash flows as impacted by the changes in the rates attributable to the market risk being measured. The discount rates used for the present value computations were selected based on market interest and foreign currency exchange rates in effect at December 30, 2012. The values that result from these computations are then compared with the market values of the financial instruments. The differences are the hypothetical gains or losses associated with each type of risk.

Interest Rate Risk

Based on a hypothetical immediate 150 basis point increase in interest rates, with all other variables held constant, the fair value of our fixed rate long-term debt would be impacted by a net decrease of $13.5 million. Conversely, a 150 basis point decrease in interest rates would result in a net increase in the fair value of our fixed rate long-term debt of $8.0 million.

Foreign Currency Exchange Rate Risk

As of December 30, 2012, a 10% decrease or increase in the levels of foreign currency exchange rates against the U.S. dollar, with all other variables held constant, would result in a decrease in the fair value of our short-term financial instruments (primarily cash, accounts receivable and accounts payable) of $9.4 million or an increase in the fair value of our financial instruments of $7.7 million, respectively. As the impact of offsetting changes in the fair market value of our net foreign investments is not included in the sensitivity model, these results are not indicative of our actual exposure to foreign currency exchange risk.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INTERFACE, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

	FISCAL YEAR 2012	2011	2010
	(in thousands, except per share data)		
Net sales	$ 932,020	$ 953,045	$ 862,314
Cost of sales	614,841	618,303	549,184
Gross profit on sales	317,179	334,742	313,130
Selling, general and administrative expenses	231,358	243,287	217,080
Restructuring and asset impairment charges	19,425	5,755	2,943
Expenses related to Australia fire	1,748	0	0
Operating income	64,648	85,700	93,107
Interest expense	25,024	26,325	33,233
Bond retirement expenses	0	0	44,379
Other expense	1,521	465	582
Income from continuing operations before tax expense	38,103	58,910	14,913
Income tax expense	15,204	20,640	4,616
Income from continuing operations	22,899	38,270	10,297
Income (loss) from discontinued operations, net of tax	(16,956)	451	(963)
Net income	5,943	38,721	9,334
Net income attributable to noncontrolling interest in subsidiary	0	0	(1,051)
Net income attributable to Interface, Inc.	$ 5,943	$ 38,721	$ 8,283
Income (loss) per share attributable to Interface, Inc. common shareholders basic			
Continuing operations	$ 0.35	$ 0.59	$ 0.14
Discontinued operations	(0.26)	0.01	(0.01)
Net income per share attributable to Interface, Inc. common shareholders basic	$ 0.09	$ 0.59	$ 0.13
Income (loss) per share attributable to Interface, Inc. common shareholders diluted			
Continuing operations	$ 0.35	$ 0.58	$ 0.14
Discontinued operations	(0.26)	0.01	(0.01)
Net income per share attributable to Interface, Inc. common shareholders diluted	$ 0.09	$ 0.59	$ 0.13
Basic weighted average common shares outstanding	65,767	65,291	63,794
Diluted weighted average common shares outstanding	65,900	65,486	64,262

See accompanying notes to consolidated financial statements.

INTERFACE, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	FISCAL YEAR 2012	2011	2010
		(in thousands)	
Net income	$ 5,943	$ 38,721	$ 9,334
Other comprehensive income (loss)			
Foreign currency translation adjustment	8,539	(7,614)	(1,754)
Pension liability adjustment	771	(5,066)	1,990
Comprehensive income	15,253	26,041	9,570
Comprehensive income attributable to noncontrolling interest	0	0	(1,509)
Comprehensive income attributable to Interface, Inc.	$ 15,253	$ 26,041	$ 8,061

See accompanying notes to consolidated financial statements.

INTERFACE, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	2012	2011
	(in thousands)	
ASSETS		
Current		
Cash and cash equivalents	$ 90,533	$ 50,624
Accounts receivable, net	137,313	140,800
Inventories	141,176	140,485
Prepaid expenses and other current assets	51,358	20,522
Deferred income taxes	10,271	9,699
Assets of businesses held for sale	0	60,683
Total current assets	430,651	422,813
Property and equipment, net	165,725	177,925
Deferred tax asset	62,856	47,290
Goodwill	75,672	74,557
Other assets	54,463	49,687
	$ 789,367	$ 772,272
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities		
Accounts payable	$ 56,292	$ 52,226
Accrued expenses	97,424	90,693
Current portion of long-term debt	8,110	0
Liabilities held for sale	0	8,269
Total current liabilities	161,826	151,188
Senior notes	275,000	283,030
Senior subordinated notes	0	11,477
Deferred income taxes	7,339	8,391
Other	49,500	37,147
Total liabilities	493,665	491,233
Commitments and contingencies		
Shareholders equity		
Preferred stock	0	0
Common stock	6,606	6,548
Additional paid-in capital	366,677	361,400
Retained deficit	(16,746)	(16,764)
Accumulated other comprehensive loss foreign currency translation	(25,344)	(33,883)
Accumulated other comprehensive loss pension liability	(35,491)	(36,262)
Total shareholders equity	295,702	281,039
	$ 789,367	$ 772,272

See accompanying notes to consolidated financial statements.

INTERFACE, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	FISCAL YEAR 2012	2011 (in thousands)	2010
OPERATING ACTIVITIES:			
Net income	$ 5,943	$ 38,721	$ 9,334
Income (loss) on discontinued operations, net of taxes	(16,956)	451	(963)
Income from continuing operations	22,899	38,270	10,297
Adjustments to reconcile income to cash provided by operating activities			
Depreciation and amortization	25,882	25,179	25,051
Stock compensation amortization expense	3,293	10,138	2,876
Premium paid to repurchase senior and senior subordinated notes	0	0	36,374
Bad debt expense	1,119	1,560	2,031
Deferred income taxes and other	(11,164)	4,549	(6,999)
Working capital changes:			
Accounts receivable	19,994	(7,453)	(21,418)
Inventories	1,075	(31,629)	(23,103)
Prepaid expenses and other current assets	(11,948)	1,359	(5,970)
Accounts payable and accrued expenses	(4,262)	(17,609)	28,241
Cash provided by operating activities	46,888	24,364	47,380
INVESTING ACTIVITIES:			
Capital expenditures	(42,428)	(38,050)	(31,715)
Other	(2,629)	(1,566)	(5,328)
Net proceeds from sale of Bentley Prince Street	32,174	0	0
Cash received from insurance company	20,718	0	0
Cash provided by (used in) investing activities	7,835	(39,616)	(37,043)
FINANCING ACTIVITIES:			
Borrowing of long-term debt	0	0	275,000
Dividends paid	(5,925)	(5,227)	(2,721)
Debt issuance costs	0	(1,025)	(5,930)
Repurchase of senior and senior subordinated notes	(11,477)	0	(279,966)
Premium paid to repurchase senior and senior subordinated notes	0	0	(36,374)
Purchase of noncontrolling interest	0	0	(11,488)
Proceeds from issuance of common stock	1,496	2,669	3,103
Cash used in financing activities	(15,906)	(3,583)	(58,376)
Net cash provided by (used in) operating, investing and financing activities	38,817	(18,835)	(48,039)
Effect of exchange rate changes on cash	1,092	234	1,912
CASH AND CASH EQUIVALENTS:			
Net increase (decrease)	39,909	(18,601)	(46,127)
Balance, beginning of year	50,624	69,225	115,352
Balance, end of year	$ 90,533	$ 50,624	$ 69,225

See accompanying notes to consolidated financial statements.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

The Company is a recognized leader in the worldwide commercial interiors market, offering modular carpet. The Company manufactures modular carpet focusing on the high quality, designer-oriented sector of the market, and provides specialized carpet replacement, installation and maintenance services. Additionally, the Company offers *Intersept*, a proprietary antimicrobial used in a number of interior finishes.

In 2012, the Company sold its Bentley Prince Street business segment to a third party. Bentley Prince Street designed, manufactured and marketed broadloom and modular carpet. The results of operations and related disposal costs, gains and losses for the Bentley Prince Street business are classified as discontinued operations for all periods presented. In addition, assets and liabilities of the Bentley Prince Street business have been reported in assets and liabilities held for sale for all reported periods.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All material intercompany accounts and transactions are eliminated. Investments in which the Company does not have the ability to exercise significant influence are carried at fair value. The Company monitors investments for other than temporary declines in value and makes reductions in carrying values when appropriate. As of December 30, 2012 and January 1, 2012, the Company did not hold significant investments of this nature.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Examples include provisions for returns, bad debts, product claims reserves, rebates, inventory obsolescence and the length of product life cycles, accruals associated with restructuring activities, income tax exposures and valuation allowances, environmental liabilities, and the carrying value of goodwill and property and equipment. Actual results could vary from these estimates.

Revenue Recognition

Revenue is recognized when the following criteria are met: persuasive evidence of an agreement exists, delivery has occurred or services have been rendered, price to the buyer is fixed and determinable, and collectability is reasonably assured. Delivery is not considered to have occurred until the customer takes title and assumes the risks and rewards of ownership, which is generally on the date of shipment. Provisions for discounts, sales returns and allowances are estimated using historical experience, current economic trends, and the Company s quality performance. The related provision is recorded as a reduction of sales and cost of sales in the same period that the revenue is recognized. Material differences may result in the amount and timing of net sales for any period if management makes different judgments or uses different estimates.

Shipping and handling fees billed to customers are classified in net sales in the consolidated statements of operations. Shipping and handling costs incurred are classified in cost of sales in the consolidated statements of operations.

Research and Development

Research and development costs are expensed as incurred and are included in the selling, general and administrative expense caption in the consolidated statements of operations. Research and development expense was $12.4 million, $12.1 million and $11.1 million for the years 2012, 2011 and 2010, respectively.

Cash, Cash Equivalents and Short-Term Investments

Highly liquid investments with insignificant interest rate risk and with original maturities of three months or less are classified as cash and cash equivalents. Investments with maturities greater than three months and less than one year are classified as short-term investments. The Company did not hold any significant amounts of short-term investments at January 1, 2012 or January 2, 2011.

Cash payments for interest amounted to approximately $23.1 million, $23.7 million and $34.3 million for the years 2012, 2011 and 2010, respectively. Income tax payments amounted to approximately $10.0 million, $19.9 million and $13.9 million for the years 2012, 2011 and 2010, respectively. During the years 2012, 2011 and 2010, the Company received income tax refunds of $0.1 million, $4.4 million and $0.8 million, respectively.

Inventories

Inventories are carried at the lower of cost (standards approximating the first-in, first-out method) or market. Costs included in inventories are based on invoiced costs and/or production costs, as applicable. Included in production costs are material, direct labor and allocated overhead. The Company writes down inventories for the difference between the carrying value of the inventories and their estimated net realizable value. If actual market conditions are less favorable than those projected by management, additional write-downs may be required.

Management estimates its reserves for inventory obsolescence by continuously examining its inventories to determine if there are indicators that carrying values exceed net realizable values. Experience has shown that significant indicators that could require the need for additional inventory write-downs are the age of the inventory, the length of its product life cycles, anticipated demand for the Company s products, and current economic conditions. While management believes that adequate write-downs for inventory obsolescence have been made in the consolidated financial statements, consumer tastes and preferences will continue to change and the Company could experience additional inventory write-downs in the future.

Rebates

The Company has agreements to receive cash consideration from certain of its vendors, including rebates and cooperative marketing reimbursements. The amounts received from its vendors are generally presumed to be a reduction of the prices the Company pays for their products and, therefore, such amounts are reflected as either a reduction of cost of sales in the accompanying consolidated statements of operations, or, if the product inventory is still on hand at the reporting date, it is reflected as a reduction of Inventories on the accompanying consolidated balance sheets. Vendor rebates are typically dependent upon reaching minimum purchase thresholds. The Company evaluates the likelihood of reaching purchase thresholds using past experience and current year forecasts. When rebates can be reasonably estimated and receipt becomes probable, the Company records a portion of the rebate as the Company makes progress towards the purchase threshold.

When the Company receives direct reimbursements for costs incurred in marketing the vendor s product or service, the amount received is recorded as an offset to selling, general and administrative expenses in the accompanying consolidated statements of operations.

Assets and Liabilities of Businesses Held for Sale

The Company considers businesses to be held for sale when the Board or management, having the relevant authority to do so, approves and commits to a formal plan to actively market a business for sale and the sale is considered probable. Upon designation as held for sale, the carrying value of the assets of the business are recorded at the lower of their carrying value or their estimated fair value, less costs to sell. The Company ceases to record depreciation expense at that time.

Property and Equipment and Long-Lived Assets

Property and equipment are carried at cost. Depreciation is computed using the straight-line method over the following estimated useful lives: buildings and improvements ten to forty years; and furniture and equipment three to twelve years. Interest costs for the construction/development of certain long-term assets are capitalized and amortized over the related assets estimated useful lives. The Company capitalized net interest costs on qualifying expenditures of approximately $0.7 million, $0.6 million and $0.6 million for the fiscal years 2012, 2011 and 2010, respectively. Depreciation expense amounted to approximately $24.2 million, $22.3 million and $18.2 million for the years 2012, 2011 and 2010, respectively.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum of the expected future undiscounted cash flow is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and carrying value of the asset. Repair and maintenance costs are charged to operating expense as incurred.

Goodwill and Other Intangible Assets

Goodwill is the excess of the purchase price over the fair value of net assets acquired in business combinations accounted for as acquisitions. Accumulated amortization amounted to approximately $77.3 million at both December 30, 2012 and January 1, 2012, and cumulative impairment losses recognized were $212.6 million as of both December 30, 2012 and January 1, 2012.

As of December 30, 2012 and January 1, 2012, the net carrying amount of goodwill was $75.7 million and $74.6 million, respectively. Other intangible assets were $2.5 million and $2.0 million as of December 30, 2012, and January 1, 2012, respectively. The Company capitalizes patent defense costs when it determines that a successful defense is probable. Any patent defense costs are amortized over the remaining useful life of the patent. Amortization expense related to intangible assets during the years 2012, 2011 and 2010 was $0.4 million, $0.7 million, and $0.4 million, respectively.

During the fourth quarters of 2012, 2011 and 2010, the Company performed the annual goodwill impairment test required by applicable accounting standards. The Company performs this test at the reporting unit level, which is one level below the segment level for the Modular Carpet segment. In effecting the impairment testing, the Company prepared valuations of reporting units on both a market comparable methodology and an income methodology in accordance with the applicable standards, and those valuations were compared with the respective book values of the reporting units to determine whether any goodwill impairment existed. In preparing the valuations, past, present and future expectations of performance were considered. The annual testing indicated no potential of goodwill impairment in any of the years presented.

Each of the Company s reporting units maintained fair values in excess of their respective carrying values as of the fourth quarter of 2012, and therefore no impairment was indicated during the impairment testing. As of December 30, 2012, if the Company s estimates of the fair values of its reporting units which carry a goodwill balance were 10% lower, the Company still believes no goodwill impairment would have existed.

The changes in the carrying amounts of goodwill for the year ended December 30, 2012 are as follows:

BALANCE JANUARY 1, 2012	ACQUISITIONS	IMPAIRMENT	FOREIGN CURRENCY TRANSLATION	BALANCE DECEMBER 30, 2012
		(in thousands)		
$ 74,557	$ 0	$ 0	$ 1,115	$ 75,672

Product Warranties

The Company typically provides limited warranties with respect to certain attributes of its carpet products (for example, warranties regarding excessive surface wear, edge ravel and static electricity) for periods ranging from ten to twenty years, depending on the particular carpet product and the environment in which it is to be installed. The Company typically warrants that services performed will be free from defects in workmanship for a period of one year following completion. In the event of a breach of warranty, the remedy typically is limited to repair of the problem or replacement of the affected product.

The Company records a provision related to warranty costs based on historical experience and periodically adjusts these provisions to reflect changes in actual experience. Warranty reserves amounted to $1.2 million and $0.9 million as of December 30, 2012 and January 1, 2012, respectively, and are included in Accrued Expenses in the accompanying consolidated balance sheets.

Taxes on Income

The Company accounts for income taxes under an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in the Company s financial statements or tax returns. In estimating future tax consequences, the Company generally considers all expected future events other than enactments of changes in tax laws or rates. The effect on deferred tax assets and liabilities of a change in tax rates will be recognized as income or expense in the period that includes the enactment date.

The Company records a valuation allowance to reduce its deferred tax assets when it is more likely than not that some portion or all of the deferred tax assets will expire before realization of the benefit or that future deductibility is not probable. The ultimate realization of the deferred tax assets depends on the ability to generate sufficient taxable income of the appropriate character in the future. This requires us to use estimates and make assumptions regarding significant future events such as the taxability of entities operating in the various taxing jurisdictions.

The Company does not record taxes collected from customers and remitted to governmental authorities on a gross basis.

For uncertain tax positions, the Company applies the provisions of relevant authoritative guidance, which requires application of a more likely than not threshold to the recognition and derecognition of tax positions. The Company s ongoing assessments of the more likely than not outcomes of tax authority examinations and related tax positions require significant judgment and can increase or decrease the Company s effective tax rate as well as impact operating results. For further information, see the Note entitled Taxes on Income.

Fair Values of Financial Instruments

Fair values of cash and cash equivalents and short-term debt approximate cost due to the short period of time to maturity. Fair values of debt are based on quoted market prices or pricing models using current market rates.

Translation of Foreign Currencies

The financial position and results of operations of the Company s foreign subsidiaries are measured generally using local currencies as the functional currency. Assets and liabilities of these subsidiaries are translated into U.S. dollars at the exchange rate in effect at each year-end. Income and expense items are translated at average exchange rates for the year. The resulting translation adjustments are recorded in the foreign currency translation adjustment account. In the event of a divestiture of a foreign subsidiary, the related foreign currency translation results are reversed from equity to income. Foreign currency exchange gains and losses are included in net income (loss). Foreign exchange translation gains (losses) were $8.5 million, ($7.6 million) and ($1.8 million) for the years 2012, 2011 and 2010, respectively.

Income (Loss) Per Share

Basic income (loss) per share is computed based on the average number of common shares outstanding. Diluted income (loss) per share reflects the increase in average common shares outstanding that would result from the assumed exercise of outstanding stock options, calculated using the treasury stock method.

Stock-Based Compensation

As of fiscal year 2012, the Company has stock-based employee compensation plans, which are described more fully in the Shareholders Equity Note below.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, with the following weighted average assumptions used for grants issued in fiscal years 2011 and 2010 (there were no stock options granted in 2012):

	FISCAL YEAR	
	2011	2010
Risk free interest rate	0.9%	2.1%
Expected option life	5.75 years	5.75 years
Expected volatility	65%	61%
Expected dividend yield	0.6%	0.4%

The weighted average fair value of stock options (as of grant date) granted during the years 2011 and 2010 was $7.37 and $6.86, respectively, per share.

The Company recognizes expense related to its restricted stock grants based on the grant date fair value of the stock issued, as determined by its market price at date of issue.

Derivative Financial Instruments

Accounting standards require a company to recognize all derivatives on the balance sheet at fair value. Derivatives that do not meet the criteria of an accounting hedge must be adjusted to fair value through income. If the derivative is a fair value hedge, changes in the fair value of the hedged assets, liabilities or firm commitments are recognized through earnings. If the derivative is a cash flow hedge, the effective portion of changes in the fair value of the derivative are recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative s change in fair value is immediately recognized in earnings. As of December 30, 2012 and January 1, 2012, the Company was not party to any significant derivative instruments.

Pension Benefits

Net pension expense recorded is based on, among other things, assumptions about the discount rate, estimated return on plan assets and salary increases. While the Company believes these assumptions are reasonable, changes in these and other factors and differences between actual and assumed changes in the present value of liabilities or assets of the Company s plans above certain thresholds could cause net annual expense to increase or decrease materially from year to year. The actuarial assumptions used in the Company s salary continuation plan and foreign defined benefit plans reporting are reviewed periodically and compared with external benchmarks to ensure that they appropriately account for our future pension benefit obligation. The expected long-term rate of return on plan assets assumption is based on weighted average expected returns for each asset class. Expected returns reflect a combination of historical performance analysis and the forward-looking views of the financial markets, and include input from actuaries, investment service firms and investment managers.

Environmental Remediation

The Company provides for remediation costs and penalties when the responsibility to remediate is probable and the amount of associated costs is reasonably determinable. Remediation liabilities are accrued based on estimates of known environmental exposures and are discounted in certain instances. The Company regularly monitors the progress of environmental remediation. Should studies indicate that the cost of remediation is to be more than previously estimated, an additional accrual would be recorded in the period in which such determination is made. As of December 30, 2012 and January 1, 2012, no significant amounts were provided for remediation liabilities.

Allowances for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of customers to make required payments. Estimating this amount requires the Company to analyze the financial strengths of its customers. If the financial condition of the Company s customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. By its nature, such an estimate is highly subjective, and it is possible that the amount of accounts receivable that the Company is unable to collect may be different than the amount initially estimated. The Company s allowance for doubtful accounts on December 30, 2012, and January 1, 2012, was $8.8 million and $8.9 million, respectively.

Reclassifications

Certain prior period amounts have been reclassified to conform to current year financial statement presentation.

Fiscal Year

The Company s fiscal year is the 52 or 53 week period ending on the Sunday nearest December 31. All references herein to 2012, 2011, and 2010, mean the fiscal years ended December 30, 2012, January 1, 2012 and January 2, 2011, respectively. Fiscal years 2012, 2011 and 2010 were each comprised of 52 weeks.

RECENT ACCOUNTING PRONOUNCEMENTS

In September 2011, the Financial Accounting Standards Board (FASB) issued an accounting standard regarding the performance of a company s annual goodwill impairment evaluation. This standard allows companies to assess qualitative factors to determine if it is more likely than not that goodwill might be impaired and whether it is necessary to perform the two-step goodwill impairment test. This standard is effective for fiscal years beginning after December 31, 2011. The adoption of this standard did not have any significant impact on the Company s consolidated financial statements.

In June 2011, the FASB amended an accounting standard regarding the presentation of comprehensive income. This amendment will require companies to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. It eliminates the option to present components of other comprehensive income as part of the statement of changes in shareholders equity. The amended guidance, which must be applied retroactively, was to be effective for interim and annual periods ending after December 31, 2012, with earlier adoption permitted. In December of 2011, the FASB issued an amendment to this statement which defers the requirements of this standard. As this amendment only effects presentation, there is not expected to be any impact on the Company s consolidated financial statements.

RECEIVABLES

The Company has adopted credit policies and standards intended to reduce the inherent risk associated with potential increases in its concentration of credit risk due to increasing trade receivables from sales to owners and users of commercial office facilities and with specifiers such as architects, engineers and contracting firms. Management believes that credit risks are further moderated by the diversity of its end customers and geographic sales areas. The Company performs ongoing credit evaluations of its customers financial condition and requires collateral as deemed necessary. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of customers to make required payments. If the financial condition of its customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. As of December 30, 2012, and January 1, 2012, the allowance for bad debts amounted to $8.8 million and $8.9 million, respectively, for all accounts receivable of the Company. Reserves for sales returns and allowances amounted to $3.1 million and $4.3 million as of December 30, 2012, and January 1, 2012, respectively.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company does not have significant assets and liabilities measured at fair value on a recurring basis under applicable accounting standards as of the end of 2012. The Company does have approximately $22.3 million of Company-owned life insurance which is measured on readily determinable cash surrender value on a recurring basis. Due to the short maturity of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, their carrying values approximate fair value. The fair value of long term debt represented by the Company s 7 5/8% Senior Notes and 11 3/8% Senior Secured Notes based on quoted market prices, was $296.5 million, and $8.1 million, respectively at December 30, 2012.

INVENTORIES

Inventories are summarized as follows:

	2012	2011
	(in thousands)	
Finished goods	$ 87,094	$ 86,970
Work-in-process	7,030	8,920
Raw materials	47,052	44,595
	$ 141,176	$ 140,485

Reserves for inventory obsolescence amounted to $12.9 million and $10.4 million as of December 30, 2012, and January 1, 2012, respectively, and have been netted against amounts presented above.

PROPERTY AND EQUIPMENT

Property and equipment consisted of the following:

	2012	2011
	(in thousands)	
Land	$ 7,714	$ 7,166
Buildings	104,296	92,204
Equipment	298,413	321,073
	410,423	420,443
Accumulated depreciation	(244,698)	(242,518)
	$ 165,725	$ 177,925

The estimated cost to complete construction-in-progress for which the Company was committed at December 30, 2012, was approximately $19.0 million.

ACCRUED EXPENSES

Accrued expenses are summarized as follows:

	2012	2011
	(in thousands)	
Compensation	$ 55,332	$ 45,635
Interest	2,202	2,584

Restructuring	4,350	4,190
Taxes	10,579	3,875
Accrued purchases	1,439	3,949
Other	23,522	30,460
	$ 97,424	$ 90,693

Other non-current liabilities include pension liability of $23.7 million and $28.8 million as of December 30, 2012, and January 1, 2012, respectively (see the discussion below in the Note entitled Employee Benefit Plans).

BORROWINGS

Domestic Revolving Credit Facility

The Company has a domestic revolving credit facility that provides for a maximum aggregate amount of loans and letters of credit of up to $100 million (with the option to increase it to a maximum of $150 million upon the satisfaction of certain conditions) at any one time, subject to the borrowing base described below. The key features of the domestic revolving credit facility are as follows:

- The revolving credit facility currently matures on June 24, 2016;
- The revolving credit facility includes a domestic U.S. dollar syndicated loan and letter of credit facility made available to Interface, Inc. up to the lesser of (1) $100 million, or (2) a borrowing base equal to the sum of specified percentages of eligible accounts receivable and inventory in the United States (the percentages and eligibility requirements for the borrowing base are specified in the credit facility), less certain reserves;
- Advances under the facility are secured by a first-priority lien on substantially all of Interface, Inc. s assets and the assets of each of its material domestic subsidiaries, which have guaranteed the revolving credit facility; and
- The revolving credit facility contains a financial covenant (a fixed charge coverage ratio test) that becomes effective in the event that the Company s excess borrowing availability falls below 12.5% of the aggregate loan commitments of the lenders. In such event, the Company must comply with the financial covenant for a period commencing on the last day of the fiscal quarter immediately preceding such event (unless such event occurs on the last day of a fiscal quarter, in which case the compliance period commences on such date) and ending on the last day of the fiscal quarter immediately following the fiscal quarter in which such event occurred.

The revolving credit facility also includes various reporting, affirmative and negative covenants, and other provisions that restrict the Company s ability to take certain actions, including provisions that restrict the Company s ability to repay its long-term indebtedness unless it meets a specified minimum excess availability test.

Interest Rates and Fees. Interest on base rate loans is charged at varying rates computed by applying a margin ranging from 0.75% to 1.25% over the applicable base interest rate (which is defined as the greatest of the prime rate, a specified federal funds rate plus 0.50%, or the one-month LIBOR rate), depending on the Company s average excess borrowing availability during the most recently completed fiscal quarter. Interest on LIBOR-based loans and fees for letters of credit are charged at varying rates computed by applying a margin ranging from 1.75% to 2.25% over the applicable LIBOR rate, depending on the Company s average excess borrowing availability during the most recently completed fiscal quarter. In addition, the Company pays an unused line fee of 0.375% per annum on the facility.

Prepayments. The revolving credit facility requires prepayment from the proceeds of certain asset sales.

Covenants. The revolving credit facility also limits the Company s ability, among other things, to:

- repay the Company s other indebtedness prior to maturity unless the Company meets a specified minimum excess availability test;
- incur indebtedness or contingent obligations;
- make acquisitions of or investments in businesses (in excess of certain specified amounts);

sell or dispose of assets (in excess of certain specified amounts);

create or incur liens on assets; and

enter into sale and leaseback transactions.

The Company is presently in compliance with all covenants under the domestic revolving credit facility and anticipates that it will remain in compliance with the covenants for the foreseeable future.

Events of Default. If the Company breaches or fails to perform any of the affirmative or negative covenants under the revolving credit facility, or if other specified events occur (such as a bankruptcy or similar event or a change of control of Interface, Inc. or certain subsidiaries, or if the Company breaches or fails to perform any covenant or agreement contained in any instrument relating to any of the Company s other indebtedness exceeding $15 million), after giving effect to any applicable notice and right to cure provisions, an event of default will exist. If an event of default exists and is continuing, the lenders agent may, and upon the written request of a specified percentage of the lender group shall:

declare all commitments of the lenders under the facility terminated;

declare all amounts outstanding or accrued thereunder immediately due and payable; and

exercise other rights and remedies available to them under the agreement and applicable law.

Collateral. The facility is secured by substantially all of the assets of Interface, Inc. and its domestic subsidiaries (subject to exceptions for certain immaterial subsidiaries), including all of the stock of the Company s domestic subsidiaries and up to 65% of the stock of its first-tier material foreign subsidiaries. If an event of default occurs under the revolving credit facility, the lenders collateral agent may, upon the request of a specified percentage of lenders, exercise remedies with respect to the collateral, including, in some instances, foreclosing mortgages on real estate assets, taking possession of or selling personal property assets, collecting accounts receivables, or exercising proxies to take control of the pledged stock of domestic and first-tier material foreign subsidiaries.

As of December 30, 2012, the Company had no borrowings outstanding under this facility. At December 30, 2012, the Company had $3.9 million outstanding in letters of credit under this facility. As of December 30, 2012, the Company could have incurred $62.8 million of additional borrowings under this facility.

Credit Agreement with The Royal Bank of Scotland N.V.

The Company s European subsidiary Interface Europe B.V. and certain of Interface Europe B.V. s subsidiaries have a Credit Agreement with The Royal Bank of Scotland N.V. (as successor to ABN AMRO Bank N.V.) (RBS). Under the Credit Agreement, RBS provides a credit facility, until further notice, for borrowings and bank guarantees of up to 20.0 million.

Interest on borrowings under the facility is charged at varying rates computed by applying a margin of 1% over RBS s euro base rate (consisting of the leading refinancing rate as determined from time to time by the European Central Bank plus a debit interest surcharge), which base rate is subject to a minimum of 3.5% per annum. Fees on bank guarantees and documentary letters of credit are charged at a rate of 1% per annum or part thereof on the maximum amount and for the maximum duration of each guarantee or documentary letter of credit issued. A facility fee of 0.5% per annum is payable with respect to the facility amount. The facility is secured by liens on certain real property, personal property and other assets of the Company s principal European subsidiaries. The facility also includes certain financial covenants (which require the borrowers and their subsidiaries to maintain a minimum interest coverage ratio, total debt/EBITDA ratio and tangible net worth/total assets) and affirmative and negative covenants, and other provisions that restrict the borrowers ability (and the ability of certain of the borrowers subsidiaries) to take certain actions. As of December 30, 2012, there were no borrowings outstanding under this facility.

The Company is presently in compliance with all covenants under this facility and anticipates that it will remain in compliance with the covenants for the foreseeable future.

7 5/8% Senior Notes

On December 3, 2010, the Company completed a private offering of $275 million aggregate principal amount of 7 5/8% Senior Notes due 2018 (the 7 5/8% Senior Notes). Interest on the 7 5/8% Senior Notes is payable semi-annually on June 1 and December 1 (the first payment was made on June 1, 2011). The Company used the net proceeds from the sale of the 7 5/8% Senior Notes (plus cash on hand) in connection with the repurchase of approximately $141.9 million aggregate principal amount of the 11.375% Senior Secured Notes and approximately $98.5 million aggregate principal amount of the former 9.5% Senior Subordinated Notes, pursuant to a tender offer the Company conducted.

The 7 5/8% Senior Notes are guaranteed, fully, unconditionally, and jointly and severally, on an unsecured senior basis by certain of the Company s domestic subsidiaries. The Company may redeem some or all of these notes at any time prior to December 1, 2014, at a redemption price equal to 100% of the principal amount plus a make-whole premium. Prior to December 1, 2014, the Company may redeem up to 10% of the aggregate principal amount of the 7 5/8% Senior Notes per 12-month period at a redemption price equal to 103% of the principal amount of the notes redeemed, plus accrued and unpaid interest. In addition, at any time prior to December 1, 2013, the Company may redeem up to 35% of the 7 5/8% Senior Notes with the net cash proceeds from specified equity offerings at a redemption price equal to 107.625% of the principal amount, plus accrued and unpaid interest, if any, to the date of redemption. In addition, the notes will become redeemable for cash after December 1, 2014 at the Company s option, in whole or in part, initially at a redemption price equal to 103.813% of the principal amount, declining to 100% of the principal amount on December 1, 2016, plus accrued interest thereon to the date fixed for redemption. As of both December 30, 2012, and January 1, 2012, the balance of the 7 5/8% Senior Notes outstanding was $275 million. The estimated fair value of the 7 5/8% Senior Notes as of December 30, 2012, and January 1, 2012, based on then current market prices, was $295.6 million and $288.8 million, respectively.

11 3/8% Senior Secured Notes

On June 5, 2009, the Company completed a private offering of $150 million aggregate principal amount of 11 3/8% Senior Secured Notes due 2013. Interest on the 11 3/8% Senior Secured Notes is payable semi-annually on May 1 and November 1 (the first payment was made on November 1, 2009). The 11 3/8% Senior Secured Notes are guaranteed, jointly and severally, on a senior secured basis by certain of the Company s domestic subsidiaries. The 11 3/8% Senior Secured Notes are secured by a second-priority lien on substantially all of the Company s and certain of the Company s domestic subsidiaries assets that secure the Company s domestic revolving credit facility on a first-priority basis.

The Company may redeem all or a part of the 11 3/8% Senior Secured Notes from time to time at a price equal to 100% of the principal amount plus a make-whole premium. As of both December 30, 2012, and January 1, 2012, the balance of the 11 3/8% Senior Secured Notes outstanding, net of the remaining unamortized original issue discount, was approximately $8.1 million. The estimated fair value of the 11 3/8% Senior Secured Notes as of both December 30, 2012, and January 1, 2012, based on then current market prices, was $8.1 million.

9.5% Senior Subordinated Notes

On February 4, 2004, the Company completed a private offering of $135 million in 9.5% Senior Subordinated Notes due 2014. Interest on these notes is payable semi-annually on February 1 and August 1 (the first payment was made on August 1, 2004). As of January 1, 2012, the Company had outstanding $11.5 million of 9.5% Senior Subordinated Notes due 2014. At January 1, 2012, the estimated fair value of these notes, based on then current market prices, was approximately $11.5 million. On April 9, 2012, the Company redeemed all of the remaining $11.5 million of these notes at a price equal to 100% of the principal amount of the notes plus accrued interest through the redemption date.

Other Lines of Credit

Subsidiaries of the Company have an aggregate of the equivalent of $18.9 million of other lines of credit available at interest rates ranging from 1% to 9%. As of December 30, 2012, and January 1, 2012, there were no borrowings outstanding under these lines of credit.

Borrowing Costs

Deferred borrowing costs, which include underwriting, legal and other direct costs related to the issuance of debt, net of accumulated amortization, were $5.4 million and $6.7 million, as of December 30, 2012, and January 1, 2012, respectively. The Company amortizes these costs over the life of the related debt. Expenses related to such costs for the years 2012, 2011 and 2010 amounted to $1.2 million, $1.4 million and $2.2 million, respectively. In addition to these expenses, the year 2010 includes $4.5 million of expense related to the write-down of debt costs associated with note repurchases.

Future Maturities

The aggregate maturities of borrowings for each of the five fiscal years subsequent to 2012, are as follows:

FISCAL YEAR	AMOUNT *(in thousands)*
2013	8,143
2014	0
2015	0
2016	0
2017	0
Thereafter	275,000
	$ 283,143

PREFERRED STOCK

The Company is authorized to designate and issue up to 5,000,000 shares of $1.00 par value preferred stock in one or more series and to determine the rights and preferences of each series, to the extent permitted by the Articles of Incorporation, and to fix the terms of such preferred stock without any vote or action by the shareholders. The issuance of any series of preferred stock may have an adverse effect on the rights of holders of common stock and could decrease the amount of earnings and assets available for distribution to holders of common stock. In addition, any issuance of preferred stock could have the effect of delaying, deferring or preventing a change in control of the Company. As of December 30, 2012, and January 1, 2012, there were no shares of preferred stock issued.

Preferred Share Purchase Rights

The Company has previously issued one purchase right (a Right) in respect of each outstanding share of Common Stock pursuant to a Rights Agreement it entered into in March 2008. Each Right entitles the registered holder of the Common Stock to purchase from the Company one one-hundredth of a share (a Unit) of Series B Participating Cumulative Preferred Stock (the Series B Preferred Stock).

The Rights may have certain anti-takeover effects. The Rights will cause substantial dilution to a person or group that acquires (without the consent of the Company s Board of Directors) 15% or more of the outstanding shares of Common Stock or if other specified events occur without the Rights having been redeemed or in the event of an exchange of the Rights for Common Stock as permitted under the Shareholder Rights Plan.

The dividend and liquidation rights of the Series B Preferred Stock are designed so that the value of one Unit of Series B Preferred Stock issuable upon exercise of each Right will approximate the same economic value as one share of Common Stock, including voting rights. The exercise price per Right is $90, subject to adjustment. Shares of Series B Preferred Stock will entitle the holder to a minimum preferential dividend of $1.00 per share, but will entitle the holder to an aggregate dividend payment of 100 times the dividend declared on each share of Common Stock. In the event of liquidation, each share of Series B Preferred Stock will be entitled to a minimum preferential liquidation payment of $1.00, plus accrued and unpaid dividends and distributions thereon, but will be entitled to an aggregate payment of 100 times the payment made per share of Common Stock. In the event of any merger, consolidation or other transaction in which Common Stock is exchanged for or changed into other stock or securities, cash or other property, each share of Series B Preferred Stock will be entitled to receive 100 times the amount received per share of Common Stock. Series B Preferred Stock is not convertible into Common Stock.

Each share of Series B Preferred Stock will be entitled to 100 votes on all matters submitted to a vote of the shareholders of the Company, and shares of Series B Preferred Stock will generally vote together as one class with the Common Stock and any other voting capital stock of the Company on all matters submitted to a vote of the Company s shareholders.

Further, whenever dividends on the Series B Preferred Stock are in arrears in an amount equal to six quarterly payments, the Series B Preferred Stock, together with any other shares of preferred stock then entitled to elect directors, shall have the right, as a single class, to elect one director until the default has been cured.

49

Prior to entering into the March 2008 Rights Agreement, the Company maintained a substantially similar Rights Agreement that was entered into in 1998.

SHAREHOLDERS EQUITY

Prior to March 5, 2012, the Company had two classes of common stock Class A Common Stock and Class B Common Stock. The Company was authorized to issue 80 million shares of $0.10 par value Class A Common Stock and 40 million shares of $0.10 par value Class B Common Stock. The Class A and Class B Common Stock had identical voting rights except for the election or removal of directors. Holders of Class B Common Stock were entitled as a class to elect a majority of the Board of Directors. Under the terms of the Class B Common Stock, its special voting rights to elect a majority of the Board members would terminate irrevocably if the total outstanding shares of Class B Common Stock ever comprised less than ten percent of the Company s total issued and outstanding shares of Class A and Class B Common Stock.

On March 5, 2012, the number of issued and outstanding shares of Class B Common Stock of the Company constituted less than 10% of the aggregate number of issued and outstanding shares of the Company s Class A Common Stock and Class B Common Stock (that is, 6,459,556 shares of an aggregate of 65,372,375 shares), as the cumulative result of varied transactions that caused the conversion of shares of Class B Common Stock into shares of Class A Common Stock. Accordingly, in accordance with the respective terms for the Class B Common Stock and the Class A Common Stock in Article V of the Company s Articles of Incorporation (the Articles), the Class A Common Stock and Class B Common Stock are now, irrevocably from March 5, 2012, a single class of Common Stock in all respects, with no distinction whatsoever between the voting rights or any other rights and privileges of the holders of Class A Common Stock and the holders of Class B Common Stock. The Company intends to eliminate uses of (or references to) the terms Class A and Class B in connection with the Common Stock, except for historical purposes or to facilitate transition by certain stock listing or administrative services organizations who are accustomed to the old designations for the Common Stock. Following the March 5, 2012 event, the Company is authorized to issue 120 million shares of $0.10 par value Common Stock.

The Company s Common Stock is traded on the Nasdaq Global Select Market under the symbol TILE.

The Company paid dividends totaling $0.09 per share during 2012, $0.08 per share during 2011, and $0.0425 per share during 2010, to each share of Common Stock. The future declaration and payment of dividends is at the discretion of the Company s Board, and depends upon, among other things, the Company s investment policy and opportunities, results of operations, financial condition, cash requirements, future prospects, and other factors that may be considered relevant at the time of the Board s determination. Such other factors include limitations contained in the agreement for its primary revolving credit facility and in the indentures for our public indebtedness, each of which specify conditions as to when any dividend payments may be made. As such, the Company may discontinue its dividend payments in the future if its Board determines that a cessation of dividend payments is proper in light of the factors indicated above.

All treasury stock is accounted for using the cost method.

The following tables depict the activity in the accounts which make up shareholders equity for the years 2012, 2011 and 2010.

	CLASS A SHARES	CLASS A AMOUNT	CLASS B SHARES	CLASS B AMOUNT	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS (DEFICIT)	PENSION LIABILITY	FOREIGN CURRENCY TRANSLATION ADJUSTMENT	NON-CONTROLLING INTEREST IN SUBSIDIARY
					(*in thousands*)				
Balance, at January 3, 2010	56,521	$ 5,649	6,774	$ 679	$ 343,348	$ (55,332)	$ (33,186)	$ (24,057)	$ 9,080
Net income	0	0	0	0	0	8,283	0	0	1,051
Conversion of common stock	159	16	(159)	(16)	0	0	0	0	0
Stock issuances under employee plans	631	64	0	0	2,726	0	0	0	0
Other issuances of common stock	0	0	530	53	6,418	0	0	0	0
Unamortized stock compensation expense related to restricted stock awards	0	0	0	0	(6,471)	0	0	0	0
Cash dividends paid	0	0	0	0	0	(2,721)	0	0	0
Forfeitures and compensation expense related to stock awards	0	0	0	0	4,540	0	0	0	0
Pension liability adjustment	0	0	0	0	0	0	1,990	0	0
Foreign currency translation adjustment	0	0	0	0	0	0	0	(2,212)	458
Dividend to Noncontrolling Interest Partner	0	0	0	0	0	0	0	0	(7,444)
Repurchase of Minority Interest	0	0	0	0	(899)	0	0	0	(3,145)
Balance, at January 2, 2011	57,311	$ 5,729	7,145	$ 716	$ 349,662	$ (49,770)	$ (31,196)	$ (26,269)	$ 0

	CLASS A SHARES	CLASS A AMOUNT	CLASS B SHARES	CLASS B AMOUNT	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS (DEFICIT)	PENSION LIABILITY	FOREIGN CURRENCY TRANSLATION ADJUSTMENT
					(in thousands)			
Balance, at January 2, 2011	57,311	$ 5,729	7,145	$ 716	$ 349,662	$ (49,770)	$ (31,196)	$ (26,269)
Net income	0	0	0	0	0	38,721	0	0
Conversion of common stock	593	59	(593)	(59)	0	0	0	0
Stock issuances under employee plans	502	50	0	0	210	0	0	0
Other issuances of common stock	0	0	527	53	11,336	0	0	0
Unamortized stock compensation expense related to restricted stock awards	0	0	0	0	(11,402)	0	0	0
Cash dividends paid	0	0	0	0	0	(5,231)	0	0
Forfeitures and compensation expense related to stock awards	0	0	0	0	11,594	0	0	0
Pension liability adjustment	0	0	0	0	0	0	(5,066)	0
Foreign currency translation adjustment	0	0	0	0	0	0	0	(7,614)
Other	0	0	0	0	0	(484)	0	0
Balance, at January 1, 2012	58,406	$ 5,839	7,078	$ 709	$ 361,400	$ (16,764)	$ (36,262)	$ (33,883)

	SHARES	AMOUNT	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS (DEFICIT)	PENSION LIABILITY	FOREIGN CURRENCY TRANSLATION ADJUSTMENT
			(in thousands)			
Balance, at January 1, 2012	65,484	$ 6,548	$ 361,400	$ (16,764)	$ (36,262)	$ (33,883)
Net income	0	0	0	5,943	0	0
Stock issuances under employee option plans	160	16	2,030	0	0	0
Other issuances of common stock	573	58	7,564	0	0	0
Unamortized stock compensation expense related to restricted stock awards	0	0	(7,610)	0	0	0
Cash dividends paid	0	0	0	(5,925)	0	0
Forfeitures and compensation expense related to stock awards	(155)	(16)	3,293	0	0	0
Pension liability adjustment	0	0	0	0	771	0
Foreign currency translation adjustment	0	0	0	0	0	8,539
Other	0	0	0	0	0	0
Balance, at December 30, 2012	66,062	$ 6,606	$ 366,677	$ (16,746)	$ (35,491)	$ (25,344)

Stock Options

The Company has an Omnibus Stock Incentive Plan (Omnibus Plan) under which a committee of independent directors is authorized to grant directors and key employees, including officers, options to purchase the Company s Common Stock. Options are exercisable for shares of Common Stock at a price not less than 100% of the fair market value on the date of grant. The options become exercisable either immediately upon the grant date or ratably over a time period ranging from one to five years from the date of the grant. The Company s options expire at the end of time periods ranging from three to ten years from the date of the grant. In May 2010, the shareholders approved an amendment and restatement of the Omnibus Plan. This amendment and restatement extended the term of the Omnibus Plan until February 2020, and set the number of shares authorized for issuance or transfer on or after the effective date of the amendment and restatement at 6,558,263 shares, except that each share issued pursuant to an award other than a stock option reduces the number of such authorized shares by 1.33 shares.

Accounting standards require that the Company measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair market value of the award. That cost will be recognized over the period in which the employee is required to provide the services the requisite service period (usually the vesting period) in exchange for the award. The grant date fair value for options and similar instruments will be estimated using option pricing models. Under accounting standards, the Company is required to select a valuation technique or option pricing model. The Company uses the Black-Scholes model. Accounting standards require that the Company estimate forfeitures for stock options and reduce compensation expense accordingly. The Company has reduced its expense by the assumed forfeiture rate and will evaluate actual experience against the assumed forfeiture rate going forward. This expense reduction is not significant to the Company.

The Company recognized stock option compensation expense of $0.5 million in 2012, $0.8 million in 2011 and $1.2 million in 2010. The remaining unrecognized compensation cost related to unvested awards at December 30, 2012, approximated $0.1 million, and the weighted average period of time over which this cost will be recognized is approximately one year. The expense for stock options is included in selling, general and administrative expense on the Company s consolidated statements of operations, as none of these stock options have been issued to production personnel.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model, with the following weighted average assumptions used for grants issued in 2010 and 2011 (there were no stock options granted in 2012):

	FISCAL YEAR	
	2011	2010
Risk free interest rate	0.9%	2.1%
Expected option life	5.75 years	5.75 years
Expected volatility	65%	61%
Expected dividend yield	0.5%	0.4%

The weighted average fair value of stock options (as of grant date) granted during the years 2011 and 2010 was $7.37 and $6.86, respectively, per share.

The following table summarizes stock options outstanding as of December 30, 2012, as well as activity during the previous fiscal year:

	Shares	Weighted Average Exercise Price
Outstanding at January 1, 2012	592,500	$ 9.12
Granted	0	0
Exercised	160,000	9.33
Forfeited or cancelled	39,000	11.78
Outstanding at December 30, 2012 (a)	393,500	$ 8.49
Exercisable at December 30, 2012 (b)	390,000	$ 8.43

(a) At December 30, 2012, the weighted-average remaining contractual life of options outstanding was 6.1 years.

(b) At December 30, 2012, the weighted-average remaining contractual life of options exercisable was 6.1 years.

At December 30, 2012, the aggregate intrinsic values of in-the-money options outstanding and options exercisable were $2.9 million and $2.9 million, respectively (the intrinsic value of a stock option is the amount by which the market value of the underlying stock exceeds the exercise price of the option).

The intrinsic value of stock options exercised in 2012, 2011 and 2010 was $0.9 million, $6.0 million and $5.5 million, respectively. The cash proceeds related to stock options exercised in 2012, 2011 and 2010 were $1.5 million, $2.7 million, and $3.1 million, respectively.

The tax benefit recognized with respect to stock options during the years 2012, 2011 and 2010 was not significant.

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding at December 30, 2012	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price	Number Exercisable at December 30, 2012	Weighted Average Exercise Price
$1.49 - 3.00	35,500	1.35	$ 2.44	35,500	$ 2.44
3.01 - 5.00	142,000	5.95	4.25	142,000	4.25
5.01 - 12.00	20,000	6.82	7.78	20,000	7.78
12.01 - 15.00	196,000	7.00	12.81	192,500	12.81
	393,500	6.1	$ 8.49	390,000	$ 8.43

Restricted Stock Awards

During fiscal years 2012, 2011 and 2010, the Company granted restricted stock awards totaling 573,000, 668,000 and 529,000, respectively, of Common Stock. These awards (or a portion thereof) vest with respect to each recipient over a two to five year period from the date of grant, provided the individual remains in the employment or service of the Company as of the vesting date. Additionally, these shares (or a portion thereof) could vest earlier upon the attainment of certain performance criteria, in the event of a change in control of the Company, or upon involuntary termination without cause.

Compensation expense related to the vesting of restricted stock was $3.3 million, $10.1 million and $2.9 million for 2012, 2011 and 2010, respectively. These grants are made primarily to executive-level personnel at the Company and, as a result, no compensation costs have been capitalized. Accounting standards require that the Company estimate forfeitures for restricted stock and reduce compensation expense accordingly. The Company has reduced its expense by the assumed forfeiture rate and will evaluate actual experience against the assumed forfeiture rate going forward. The forfeiture rate has been developed using historical data regarding actual forfeitures as well as an estimate of future expected forfeitures under our restricted stock grants.

The following table summarizes restricted stock activity as of December 30, 2012, and during the previous fiscal year:

	Shares	Weighted Average Grant Date Fair Value
Outstanding at		