

INTERFACE INC  
Form 10-Q  
August 09, 2012  
Table of Contents

# SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

## FORM 10-Q

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For Quarterly Period Ended July 1, 2012

Commission File Number 001-33994

## INTERFACE, INC.

(Exact name of registrant as specified in its charter)

**GEORGIA**  
(State or other jurisdiction of

**58-1451243**  
(I.R.S. Employer

incorporation or organization)

Identification No.)

**2859 PACES FERRY ROAD, SUITE 2000, ATLANTA, GEORGIA 30339**

(Address of principal executive offices and zip code)

Edgar Filing: INTERFACE INC - Form 10-Q

(770) 437-6800

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Shares outstanding of each of the registrant's classes of common stock at August 1, 2012:

Class	Number of Shares
Common Stock, \$.10 par value per share	65,967,061

**Table of Contents**

INTERFACE, INC.

INDEX

	<b>PAGE</b>
<b>PART I. FINANCIAL INFORMATION</b>	
Item 1. <u>Financial Statements</u>	3
<u>Consolidated Condensed Balance Sheets July 1, 2012 and January 1, 2012</u>	3
<u>Consolidated Condensed Statements of Operations Three Months and Six Months Ended July 1, 2012 and July 3, 2011</u>	4
<u>Consolidated Statements of Comprehensive Income (Loss) Three Months and Six Months Ended July 1, 2012 and July 3, 2011</u>	5
<u>Consolidated Condensed Statements of Cash Flows Six Months Ended July 1, 2012 and July 3, 2011</u>	6
<u>Notes to Consolidated Condensed Financial Statements</u>	7
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	20
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	25
Item 4. <u>Controls and Procedures</u>	25
<b>PART II. OTHER INFORMATION</b>	
Item 1. <u>Legal Proceedings</u>	26
Item 1A. <u>Risk Factors</u>	26
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	26
Item 3. <u>Defaults Upon Senior Securities</u>	26
Item 4. <u>Mine Safety Disclosures</u>	26
Item 5. <u>Other Information</u>	26
Item 6. <u>Exhibits</u>	26

**Table of Contents**

## PART I FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## INTERFACE, INC. AND SUBSIDIARIES

## CONSOLIDATED CONDENSED BALANCE SHEETS

(IN THOUSANDS)

	JULY 1, 2012 (UNAUDITED)	JANUARY 1, 2012
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and Cash Equivalents	\$ 36,878	\$ 50,635
Accounts Receivable, net	141,132	156,170
Inventories	173,684	166,073
Prepaid Expenses and Other Current Assets	25,578	23,407
Deferred Income Taxes	10,442	9,699
<b>TOTAL CURRENT ASSETS</b>	<b>387,714</b>	<b>405,984</b>
PROPERTY AND EQUIPMENT, less accumulated depreciation	190,652	190,119
DEFERRED TAX ASSET	46,419	47,290
GOODWILL	72,132	74,557
OTHER ASSETS	54,653	54,322
<b>TOTAL ASSETS</b>	<b>\$ 751,570</b>	<b>\$ 772,272</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts Payable	\$ 56,891	\$ 55,289
Accrued Expenses	85,072	93,884
<b>TOTAL CURRENT LIABILITIES</b>	<b>141,963</b>	<b>149,173</b>
SENIOR NOTES	283,070	283,030
SENIOR SUBORDINATED NOTES		11,477
DEFERRED INCOME TAXES	8,485	8,391
OTHER	37,188	39,162
<b>TOTAL LIABILITIES</b>	<b>470,706</b>	<b>491,233</b>
Commitments and Contingencies		
<b>SHAREHOLDERS' EQUITY:</b>		
Preferred Stock		
Common Stock	6,596	6,548
Additional Paid-In Capital	364,376	361,400
Retained Earnings (Deficit)	(15,067)	(16,764)
Accumulated Other Comprehensive Loss - Foreign Currency Translation Adjustment	(38,745)	(33,883)
Accumulated Other Comprehensive Loss - Pension Liability	(36,296)	(36,262)
<b>TOTAL SHAREHOLDERS' EQUITY</b>	<b>280,864</b>	<b>281,039</b>
	<b>\$ 751,570</b>	<b>\$ 772,272</b>

Edgar Filing: INTERFACE INC - Form 10-Q

See accompanying notes to consolidated condensed financial statements.

**Table of Contents**

INTERFACE, INC. AND SUBSIDIARIES  
CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS  
(UNAUDITED)  
(IN THOUSANDS EXCEPT PER SHARE AMOUNTS)

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JULY 1, 2012	JULY 3, 2011	JULY 1, 2012	JULY 3, 2011
NET SALES	\$ 254,607	\$ 267,640	\$ 487,367	\$ 513,042
Cost of Sales	170,012	172,865	326,569	331,339
GROSS PROFIT ON SALES	84,595	94,775	160,798	181,703
Selling, General and Administrative Expenses	62,562	68,638	121,930	134,038
Restructuring and Asset Impairment Charge			16,316	
OPERATING INCOME	22,033	26,137	22,552	47,665
Interest Expense	6,139	6,783	12,792	13,439
Other Expense	274	171	711	49
INCOME BEFORE INCOME TAX EXPENSE	15,620	19,183	9,049	34,177
Income Tax Expense	5,362	6,369	4,725	11,539
NET INCOME	\$ 10,258	\$ 12,814	\$ 4,324	\$ 22,638
Earnings Per Share Basic	\$ 0.16	\$ 0.20	\$ 0.07	\$ 0.35
Earnings Per Share Diluted	\$ 0.16	\$ 0.20	\$ 0.07	\$ 0.35
Common Shares Outstanding Basic	65,952	65,398	65,701	65,108
Common Shares Outstanding Diluted	66,128	65,677	65,868	65,363

See accompanying notes to consolidated condensed financial statements.

**Table of Contents**

INTERFACE, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)  
 (UNAUDITED)  
 (IN THOUSANDS)

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	JULY 1, 2012	JULY 3, 2011	JULY 1, 2012	JULY 3, 2011
Net Income	\$ 10,258	\$ 12,814	\$ 4,324	\$ 22,638
Other Comprehensive Income (Loss), Foreign Currency Translation Adjustment and Pension Liability Adjustment	(11,879)	4,092	(4,896)	12,358
<b>Comprehensive Income (Loss)</b>	<b>\$ (1,621)</b>	<b>\$ 16,906</b>	<b>\$ (572)</b>	<b>\$ 34,996</b>

See accompanying notes to consolidated condensed financial statements.

**Table of Contents**

INTERFACE, INC. AND SUBSIDIARIES  
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(IN THOUSANDS)

	SIX MONTHS ENDED	
	JULY 1, 2012	JULY 3, 2011
<b>OPERATING ACTIVITIES:</b>		
Net Income	\$ 4,324	\$ 22,638
Adjustments to Reconcile Net Income to Cash Provided by (Used in) Operating Activities:		
Depreciation and Amortization	12,650	13,112
Stock Compensation Amortization Expense	2,164	8,120
Deferred Income Taxes and Other	(2,356)	3,276
Working Capital Changes:		
Accounts Receivable	14,751	(7,995)
Inventories	(9,606)	(30,010)
Prepaid Expenses and Other Current Assets	(2,524)	(4,083)
Accounts Payable and Accrued Expenses	4,026	(26,442)
<b>CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:</b>	<b>23,429</b>	<b>(21,384)</b>
<b>INVESTING ACTIVITIES:</b>		
Capital Expenditures	(21,747)	(18,814)
Other	(1,137)	(1,995)
<b>CASH USED IN INVESTING ACTIVITIES:</b>	<b>(22,884)</b>	<b>(20,809)</b>
<b>FINANCING ACTIVITIES:</b>		
Repurchase of Senior Subordinated Notes	(11,477)	
Other		(505)
Proceeds from Issuance of Common Stock	131	2,579
Dividends Paid	(2,627)	(2,612)
<b>CASH USED IN FINANCING ACTIVITIES:</b>	<b>(13,973)</b>	<b>(538)</b>
<b>Net Cash Used in Operating, Investing and Financing Activities</b>	<b>(13,428)</b>	<b>(42,731)</b>
Effect of Exchange Rate Changes on Cash	(329)	794
<b>CASH AND CASH EQUIVALENTS:</b>		
Net Change During the Period	(13,757)	(41,937)
Balance at Beginning of Period	50,635	69,236
Balance at End of Period	\$ 36,878	\$ 27,299

See accompanying notes to consolidated condensed financial statements.



**Table of Contents**

## INTERFACE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

## NOTE 1 CONDENSED FOOTNOTES

As contemplated by the Securities and Exchange Commission (the Commission) instructions to Form 10-Q, the following footnotes have been condensed and, therefore, do not contain all disclosures required in connection with annual financial statements. Reference should be made to the Company's year-end audited consolidated financial statements and notes thereto contained in its Annual Report on Form 10-K for the fiscal year ended January 1, 2012, as filed with the Commission.

The financial information included in this report has been prepared by the Company, without audit. In the opinion of management, the financial information included in this report contains all adjustments (all of which are normal and recurring) necessary for a fair presentation of the results for the interim periods. Nevertheless, the results shown for interim periods are not necessarily indicative of results to be expected for the full year. The January 1, 2012, consolidated condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States.

As described below in Note 9, the Company has sold its Fabrics Group business segment. The results of operations and related disposal costs, gains and losses for this business are classified as discontinued operations, where applicable.

Certain prior period amounts have been reclassified to conform to the current period presentation.

## NOTE 2 INVENTORIES

Inventories are summarized as follows:

	July 1, 2012	January 1, 2012
	(In thousands)	
Finished Goods	\$ 101,867	\$ 98,894
Work in Process	21,201	17,606
Raw Materials	50,616	49,573
	\$ 173,684	\$ 166,073

## NOTE 3 EARNINGS PER SHARE

The Company computes basic earnings per share (EPS) by dividing net income by the weighted average common shares outstanding, including participating securities outstanding, during the period as discussed below. Diluted EPS reflects the potential dilution beyond shares for basic EPS that could occur if securities or other contracts to issue common stock were exercised, converted into common stock or resulted in the issuance of common stock that would have shared in the Company's earnings.

The Company includes all unvested stock awards which contain non-forfeitable rights to dividends or dividend equivalents, whether paid or unpaid, in the number of shares outstanding in our basic and diluted EPS calculations when the inclusion of these shares would be dilutive. Unvested share-based awards of restricted stock are paid dividends equally with all other shares of common stock. As a result, the Company includes all outstanding restricted stock awards in the calculation of basic and diluted EPS. Distributed earnings include common stock dividends and dividends earned on unvested share-based payment awards. Undistributed earnings represent earnings that were available for distribution but were not distributed. The following tables show distributed and undistributed earnings:

**Table of Contents**

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
<b>Earnings Per Share</b>				
Basic Earnings Per Share:				
Distributed Earnings	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.04
Undistributed Earnings	0.14	0.18	0.03	0.31
<b>Total</b>	<b>\$ 0.16</b>	<b>\$ 0.20</b>	<b>\$ 0.07</b>	<b>\$ 0.35</b>
Diluted Earnings Per Share:				
Distributed Earnings	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.04
Undistributed Earnings	0.14	0.18	0.03	0.31
<b>Total</b>	<b>\$ 0.16</b>	<b>\$ 0.20</b>	<b>\$ 0.07</b>	<b>\$ 0.35</b>

The following tables present net income that was attributable to participating securities:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
(In millions)				
Net Income	\$ 0.3	\$ 0.3	\$ 0.1	\$ 0.6

The weighted average shares outstanding for basic and diluted EPS were as follows:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
(In thousands)				
Weighted Average Shares Outstanding	63,927	63,623	63,676	63,333
Participating Securities	2,025	1,775	2,025	1,775
Shares for Basic Earnings Per Share	65,952	65,398	65,701	65,108
Dilutive Effect of Stock Options	176	279	167	255
Shares for Diluted Earnings Per Share	66,128	65,677	65,868	65,363

For the three-month periods ended July 1, 2012, and July 3, 2011, options to purchase 274,000 and 20,000 shares of common stock, respectively, were not included in the computation of diluted EPS as their impact would be anti-dilutive. For the six-month periods ended July 1, 2012, and July 3, 2011, options to purchase 274,000 and 20,000 shares of common stock, respectively, were not included in the computation of diluted EPS as their impact would be anti-dilutive.

**NOTE 4 SEGMENT INFORMATION**

Based on the quantitative thresholds specified by accounting standards, the Company has determined that it has two reportable segments: (1) the Modular Carpet segment, which includes its Interface, InterfaceFLOR, Heuga and FLOR modular carpet businesses, and (2) the Bentley Prince Street segment, which includes its Bentley Prince Street broadloom, modular carpet and area rug businesses. In 2007, the Company sold its former Fabrics Group business segment (see Note 9 for further information). Accordingly, the Company has included the operations of the former Fabrics Group segment in discontinued operations, where applicable.



**Table of Contents**

The accounting policies of the operating segments are the same as those described in the Summary of Significant Accounting Policies contained in the Company's Annual Report on Form 10-K for the fiscal year ended January 1, 2012, as filed with the Commission. Segment amounts disclosed are prior to any elimination entries made in consolidation, except in the case of net sales, where intercompany sales have been eliminated. The chief operating decision-maker evaluates performance of the segments based on operating income. Costs excluded from this profit measure primarily consist of allocated corporate expenses, interest/other expense and income taxes. Corporate expenses are primarily comprised of corporate overhead expenses. Thus, operating income includes only the costs that are directly attributable to the operations of the individual segment. Assets not identifiable to any individual segment are corporate assets, which are primarily comprised of cash and cash equivalents, short-term investments, intangible assets and intercompany amounts, which are eliminated in consolidation.

*Segment Disclosures*

Summary information by segment follows:

	<b>Modular Carpet</b>	<b>Bentley Prince Street (In thousands)</b>	<b>Total</b>
<b>Three Months Ended July 1, 2012</b>			
Net Sales	\$ 229,546	\$ 25,061	\$ 254,607
Depreciation and Amortization	6,010	562	6,572
Operating Income (Loss)	24,034	(1,232)	22,802
<b>Three Months Ended July 3, 2011</b>			
Net Sales	\$ 240,566	\$ 27,074	\$ 267,640
Depreciation and Amortization	6,700	565	7,265
Operating Income	26,937	96	27,033

	<b>Modular Carpet</b>	<b>Bentley Prince Street (In thousands)</b>	<b>Total</b>
<b>Six Months Ended July 1, 2012</b>			
Net Sales	\$ 439,562	\$ 47,805	\$ 487,367
Depreciation and Amortization	12,371	1,099	13,470
Operating Income (Loss)	25,086	(1,796)	23,290
<b>Six Months Ended July 3, 2011</b>			
Net Sales	\$ 459,846	\$ 53,196	\$ 513,042
Depreciation and Amortization	14,803	1,123	15,926
Operating Income (Loss)	52,271	(61)	52,210

A reconciliation of the Company's total segment operating income, depreciation and amortization, and assets to the corresponding consolidated amounts follows:

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>July 1, 2012</b>	<b>July 3, 2011</b>	<b>July 1, 2012</b>	<b>July 3, 2011</b>
	<b>(In thousands)</b>		<b>(In thousands)</b>	
<b>DEPRECIATION AND AMORTIZATION</b>				
Total segment depreciation and amortization	\$ 6,572	\$ 7,265	\$ 13,470	\$ 15,926
Corporate depreciation and amortization	698	1,385	1,344	5,306
Reported depreciation and amortization	\$ 7,270	\$ 8,650	\$ 14,814	\$ 21,232
<b>OPERATING INCOME</b>				
Total segment operating income	\$ 22,802	\$ 27,033	\$ 23,290	\$ 52,210

Edgar Filing: INTERFACE INC - Form 10-Q

Corporate income, expenses and other reconciling amounts	(769)	(896)	(738)	(4,545)
Reported operating income	\$ 22,033	\$ 26,137	\$ 22,552	\$ 47,665

-9-

**Table of Contents**

	July 1, 2012	January 1, 2012
	(In thousands)	
<b>ASSETS</b>		
Total segment assets	\$ 644,061	\$ 658,190
Corporate assets and eliminations	107,509	114,082
Reported total assets	\$ 751,570	\$ 772,272

**NOTE 5 LONG-TERM DEBT***7 5/8% Senior Notes*

As of both July 1, 2012, and July 3, 2011, the Company had outstanding \$275 million in 7 5/8% Senior Notes due 2018 (the 7 5/8% Senior Notes). The estimated fair value of the 7 5/8% Senior Notes as of July 1, 2012, and July 3, 2011, based on then current market prices, was \$292.2 million and \$288.1 million, respectively.

*11 3/8% Senior Secured Notes*

As of July 1, 2012, and July 3, 2011, the Company had outstanding \$8.1 million and \$8.0 million, respectively, in 11 3/8% Senior Secured Notes due 2013 (the 11 3/8% Senior Secured Notes). The estimated fair value of the 11 3/8% Senior Secured Notes as of July 1, 2012, and July 3, 2011, based on then current market prices, was \$8.8 million and \$8.1 million, respectively.

*9.5% Senior Subordinated Notes*

On April 9, 2012, the Company redeemed all of the remaining \$11.5 million of its outstanding 9.5% Senior Subordinated Notes due 2014 at a price equal to 100% of the principal amount of the notes, plus accrued interest through the redemption date.

*Credit Facilities*

The Company maintains a domestic revolving credit agreement (the Facility) that provides a maximum aggregate amount of \$100 million of loans and letters of credit available to us at any one time (subject to a borrowing base) with an option for us to increase that maximum aggregate amount to \$150 million (upon the satisfaction of certain conditions, and subject to a borrowing base). The Company is presently in compliance with all covenants under the Facility and anticipates that it will remain in compliance with the covenants for the foreseeable future. As of July 1, 2012, there were zero borrowings and \$3.9 million in letters of credit outstanding under the Facility. As of July 1, 2012, the Company could have incurred \$84.3 million of additional borrowings under the Facility.

Interface Europe B.V. (the Company's modular carpet subsidiary based in the Netherlands) and certain of its subsidiaries maintain a Credit Agreement with The Royal Bank of Scotland N.V. (RBS). Under this Credit Agreement, RBS provides a credit facility, until further notice, for borrowings and bank guarantees of 20 million. As of July 1, 2012, there were no borrowings outstanding under this facility, and the Company could have incurred 20 million (approximately \$24.9 million) of additional borrowings under the facility.

Other non-U.S. subsidiaries of the Company have an aggregate of the equivalent of \$18.5 million of lines of credit available. As of July 1, 2012, there were no borrowings outstanding under these lines of credit.

**NOTE 6 STOCK-BASED COMPENSATION***Stock Option Awards*

In accordance with accounting standards, the Company measures the cost of employee services received in exchange for an award of equity instruments based on the grant date fair 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 that meets the criteria stated in the standard. 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 stock compensation expense by the assumed forfeiture rate and will evaluate experience against this forfeiture rate going forward.



**Table of Contents**

During the first six months of 2012 and 2011, the Company recognized stock option compensation costs of \$0.4 million and \$0.6 million, respectively. In the second quarters of 2012 and 2011, the Company recognized stock option compensation costs of \$0.2 million and \$0.3 million, respectively. The remaining unrecognized compensation cost related to unvested awards at July 1, 2012, approximated \$0.2 million, and the weighted average period of time over which this cost will be recognized is approximately one year.

The following table summarizes stock options outstanding as of July 1, 2012, as well as activity during the six months then ended:

	Shares	Weighted Average Exercise Price
Outstanding at January 1, 2012	592,500	\$ 9.12
Granted		
Exercised	23,500	\$ 5.59
Forfeited or canceled	34,000	\$ 11.72
Outstanding at July 1, 2012	535,000	\$ 8.85
Exercisable at July 1, 2012	419,200	\$ 7.80

At July 1, 2012, the aggregate intrinsic value of in-the-money options outstanding and options exercisable was \$2.6 million and \$2.5 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).

Cash proceeds and intrinsic value related to total stock options exercised during the first six months of fiscal years 2012 and 2011 are provided in the table below. The Company did not recognize any significant tax benefit with regard to stock options in either period presented.

	Six Months Ended	
	July 1, 2012	July 3, 2011
	(In thousands)	
Proceeds from stock options exercised	\$ 131	\$ 2,579
Intrinsic value of stock options exercised	179	5,819

*Restricted Stock Awards*

During the six months ended July 1, 2012, and July 3, 2011, the Company granted restricted stock awards for 573,500 and 668,000 shares, 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, awards (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 restricted stock grants was \$2.2 million and \$8.1 million for the six months ended July 1, 2012, and July 3, 2011, respectively. 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 experience against this forfeiture rate going forward.

The following table summarizes restricted stock activity as of July 1, 2012, and during the six months then ended:

	Shares	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2012	1,749,000	\$ 15.08



Edgar Filing: INTERFACE INC - Form 10-Q

Granted	573,500	13.25
Vested	241,500	13.20
Forfeited or canceled	56,000	15.11
Outstanding at July 1, 2012	2,025,000	\$ 14.79

-11-

**Table of Contents**

As of July 1, 2012, the unrecognized total compensation cost related to unvested restricted stock was approximately \$13.9 million. That cost is expected to be recognized by the end of 2015.

For the six months ended July 1, 2012, and July 3, 2011, the Company recognized tax benefits with regard to restricted stock of \$0.3 million and \$2.1 million, respectively.

**NOTE 7 EMPLOYEE BENEFIT PLANS**

The following tables provide the components of net periodic benefit cost for the three-month and six-month periods ended July 1, 2012, and July 3, 2011, respectively:

<b>Defined Benefit Retirement Plan (Europe)</b>	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>July 1, 2012</b>	<b>July 3, 2011</b>	<b>July 1, 2012</b>	<b>July 3, 2011</b>
	<b>(In thousands)</b>		<b>(In thousands)</b>	
Service cost	\$ 113	\$ 74	\$ 229	\$ 145
Interest cost	2,542	2,932	5,086	5,770
Expected return on assets	(2,817)	(3,041)	(5,638)	(5,975)
Amortization of prior service costs	13	21	26	42
Recognized net actuarial losses	231	155	460	305
Net periodic benefit cost	\$ 82	\$ 141	\$ 163	\$ 287

<b>Salary Continuation Plan (SCP)</b>	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>July 1, 2012</b>	<b>July 3, 2011</b>	<b>July 1, 2012</b>	<b>July 3, 2011</b>
	<b>(In thousands)</b>		<b>(In thousands)</b>	
Service cost	\$ 113	\$ 98	\$ 226	\$ 196
Interest cost	254	284	507	568
Amortization of transition obligation		55		110
Amortization of prior service cost	12	12	24	24
Amortization of loss	67	95	134	185
Net periodic benefit cost	\$ 446	\$ 544	\$ 891	\$ 1,083

**NOTE 8 RESTRUCTURING CHARGES***2012 Restructuring Charge*

In the first quarter of 2012, the Company committed to a new restructuring plan in its continuing efforts to reduce costs across its worldwide operations and more closely align its operations with reduced demand levels in certain markets. The plan primarily consists of ceasing manufacturing and warehousing operations at its facility in Shelf, England. In connection with this restructuring plan, the Company incurred a pre-tax restructuring and asset impairment charge in the first quarter of 2012 in an amount of \$16.3 million. The charge is comprised of employee severance expenses of \$5.4 million, other related exit costs of \$1.6 million, and a charge for impairment of assets of approximately \$9.3 million. Approximately \$7 million of the charge will result in cash expenditures, primarily severance expense. Actions and expenses related to this plan were substantially completed by the end of the second quarter of 2012.

A summary of these restructuring activities is presented below:

<b>Total Restructuring Charge</b>	<b>Costs Incurred in 2012</b>	<b>Balance at July 1, 2012</b>
-----------------------------------	-------------------------------	--------------------------------

Edgar Filing: INTERFACE INC - Form 10-Q

		<i>(In thousands)</i>	
Workforce Reduction	5,356	1,843	3,513
Fixed Asset Impairment	9,364	9,364	
Other Related Exit Costs	1,596		1,596

-12-

**Table of Contents**

The table below details these restructuring activities by segment:

	Modular Carpet	Bentley Prince Street	Corporate	Total
		<i>(In thousands)</i>		
Total amounts expected to be incurred	\$ 16,316	\$	\$	\$ 16,316
Cumulative amounts incurred to date	11,207			11,207
Total amounts incurred in 2012	11,207			11,207

**2011 Restructuring Charge**

In the fourth quarter of 2011, the Company committed to a restructuring plan intended to reduce costs across its worldwide operations and more closely align its operations with reduced demand in certain markets. As a result of this plan, the Company incurred pre-tax restructuring and asset impairment charges of \$6.2 million in the fourth quarter of 2011. The majority of this charge (\$5.4 million) relates to the severance of approximately 110 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 \$5.4 million of this charge will result in cash expenditures, primarily severance expenses. Actions and expenses related to this plan were substantially completed by the end of 2011.

A summary of these restructuring activities is presented below:

	Restructuring Charge	Costs Incurred in 2011	Costs Incurred in 2012	Balance at July 1, 2012
		<i>(In thousands)</i>		
Workforce Reduction	5,401	1,147	2,572	1,682
Fixed Asset Impairment	776	776		

The table below details these restructuring activities by segment:

	Modular Carpet	Bentley Prince Street	Corporate	Total
		<i>(In thousands)</i>		
Total amounts expected to be incurred	\$ 5,755	\$ 422	\$	\$ 6,177
Cumulative amounts incurred to date	4,073	422		4,495
Total amounts incurred in 2012	2,430	142		2,572

**NOTE 9 DISCONTINUED OPERATIONS**

In 2007, the Company sold its Fabrics Group business segment. All activity related to this business has been included in discontinued operations, where applicable. Assets and liabilities of this business segment have been reported in assets and liabilities held for sale, where applicable.

Discontinued operations had no net sales and no net income or loss in either of the three-month or six-month periods ended July 1, 2012 and July 3, 2011.

**NOTE 10 SUPPLEMENTAL CASH FLOW INFORMATION**

Cash payments for interest amounted to \$12.0 million and \$11.2 million for the six months ended July 1, 2012, and July 3, 2011, respectively. Income tax payments amounted to \$6.0 million and \$11.1 million for the six months ended July 1, 2012, and July 3, 2011, respectively.



---

**Table of Contents**

**NOTE 11 RECENTLY ISSUED 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 affects presentation, there is not expected to be any impact on the Company s consolidated financial statements.

**NOTE 12 INCOME TAXES**

Accounting standards require that all tax positions be analyzed using a two-step approach. The first step requires an entity to determine if a tax position is more-likely-than-not to be sustained upon examination. In the second step, the tax benefit is measured as the largest amount of benefit, determined on a cumulative probability basis, that is more-likely-than-not to be realized upon ultimate settlement. In the first six months of 2012, the Company increased its liability for unrecognized tax benefits by \$0.1 million. As of July 1, 2012, the Company had accrued approximately \$7.8 million for unrecognized tax benefits.

**NOTE 13 SHARE CONVERSION**

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 (that is, on that date, 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 future 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.

**NOTE 14 SUBSEQUENT EVENT FIRE AT AUSTRALIAN MANUFACTURING FACILITY**

On July 20, 2012, subsequent to the end of the second quarter of 2012, a fire occurred at the Company s manufacturing facility in Picton, Australia. The facility s carpet production line, primarily comprised of tufting and backing machinery, sustained substantial damage and will be inoperable for an undetermined period of time. Other areas of the Company s Picton site relating to yarn preparation and warehousing were undamaged by the fire. The finished goods inventory and some raw materials for the business are kept at separate offsite locations and were not affected by this incident.

The Picton facility serves the Company s customers throughout Australia and New Zealand. It represents approximately 7% of the Company s total annual production, 10% of its net sales, and 13% of its operating income. The Company will utilize adequate production capacity at its manufacturing facilities in Thailand and China to meet customer demand typically serviced from Picton. The Company does not expect any significant inconvenience to customers. The Company has business interruption and property damage insurance.

**Table of Contents**

NOTE 15 SUBSEQUENT EVENT PENDING SALE OF BENTLEY PRINCE STREET

On July 25, 2012, the Company entered into a Stock Purchase Agreement with an affiliate of Dominus Capital, L.P., a private equity investment firm, for the sale of the Company's Bentley Prince Street business segment. The aggregate purchase price under the Agreement would be \$35.0 million paid in cash at the closing of the transaction, subject to possible working capital and/or other similar adjustments. The Company expects the closing of the transaction to occur in August of 2012. As of the end of the second quarter of 2012, Bentley Prince Street had net assets of approximately \$49 million. The Company expects to record exit costs related to the divestiture of approximately \$7-\$9 million. The final loss on disposal will be calculated based on the ending balance sheet of Bentley Prince Street as of the date of closing.

NOTE 16 SUPPLEMENTAL CONDENSED CONSOLIDATING GUARANTOR FINANCIAL STATEMENTS

The Guarantor Subsidiaries, which consist of the Company's principal domestic subsidiaries, are guarantors of the Company's 11 3/8% Senior Secured Notes due 2013 and its 7 5/8% Senior Notes due 2018. These guarantees are full and unconditional. The Supplemental Guarantor Financial Statements are presented herein pursuant to requirements of the Commission.

**Table of Contents**

INTERFACE, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS  
FOR THE THREE MONTHS ENDED JULY 1, 2012

	GUARANTOR SUBSIDIARIES	NON- GUARANTOR SUBSIDIARIES	INTERFACE, INC. (PARENT CORPORATION) (In thousands)	CONSOLIDATION AND ELIMINATION ENTRIES	CONSOLIDATED TOTALS
Net sales	\$ 167,714	\$ 117,526	\$	\$ (30,633)	\$ 254,607
Cost of sales	121,595	79,050		(30,633)	170,012
Gross profit on sales	46,119	38,476			84,595
Selling, general and administrative expenses	29,477	27,063	6,022		62,562
Operating income (loss)	16,642	11,413	(6,022)		22,033
Interest/Other expense	11,007	2,870	(7,464)		6,413
Income before taxes on income and equity in income of subsidiaries	5,635	8,543	1,442		15,620
Income tax expense	1,934	2,933	495		5,362
Equity in income (loss) of subsidiaries			9,311	(9,311)	
Net income (loss)	\$ 3,701	\$ 5,610	\$ 10,258	\$ (9,311)	\$ 10,258



**Table of Contents**

## CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

FOR THE SIX MONTHS ENDED JULY 1, 2012

	GUARANTOR SUBSIDIARIES	NON- GUARANTOR SUBSIDIARIES	INTERFACE, INC. (PARENT CORPORATION) (In thousands)	CONSOLIDATION AND ELIMINATION ENTRIES	CONSOLIDATED TOTALS
Net sales	\$ 310,498	\$ 238,181	\$	\$ (61,312)	\$ 487,367
Cost of sales	227,938	159,943		(61,312)	326,569
Gross profit on sales	82,560	78,238			160,798
Selling, general and administrative expenses	56,296	54,668	10,966		121,930
Restructuring and asset impairment charge	1,143	15,173			16,316
Operating income (loss)	25,121	8,397	(10,966)		22,552
Interest/Other expense	18,242	6,603	(11,342)		13,503
Income (loss) before taxes on income and equity in income of subsidiaries	6,879	1,794	376		9,049
Income tax expense	2,055	2,278	392		4,725
Equity in income (loss) of subsidiaries			4,340	(4,340)	
Net income (loss)	\$ 4,824	\$ (484)	\$ 4,324	\$ (4,340)	\$ 4,324

-17-

**Table of Contents**

## CONDENSED CONSOLIDATING BALANCE SHEET

JULY 1, 2012

	GUARANTOR SUBSIDIARIES	NON- GUARANTOR SUBSIDIARIES	INTERFACE, INC. (PARENT CORPORATION) (In thousands)	CONSOLIDATION AND ELIMINATION ENTRIES	CONSOLIDATED TOTALS
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ 1,446	\$ 26,419	\$ 9,013	\$	\$ 36,878
Accounts receivable	66,614	73,936	582		141,132
Inventories	98,789	74,895			173,684
Prepays and deferred income taxes	8,993	17,926	9,101		36,020
<b>Total current assets</b>	<b>175,842</b>	<b>193,176</b>	<b>18,696</b>		<b>387,714</b>
Property and equipment less accumulated depreciation	83,319	103,735	3,598		190,652
Investment in subsidiaries	267,400	198,892	124,800	(591,092)	
Goodwill	6,955	65,177			72,132
Other assets	5,680	10,552	84,840		101,072
	\$ 539,196	\$ 571,532	\$ 231,934	\$ (591,092)	\$ 751,570
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>					
Current liabilities	\$ 47,794	\$ 75,227	\$ 18,942	\$	\$ 141,963
Senior notes			283,070		283,070
Deferred income taxes	188	11,302	(3,005)		8,485
Other	1,406	8,565	27,217		37,188
<b>Total liabilities</b>	<b>49,388</b>	<b>95,094</b>	<b>326,224</b>		<b>470,706</b>
Common stock	94,145	102,199	6,596	(196,344)	6,596
Additional paid-in capital	249,302	12,525	364,376	(261,827)	364,376
Retained earnings (deficit)	148,441	425,226	(455,813)	(132,921)	(15,067)
Foreign currency translation adjustment	(2,080)	(29,647)	(7,018)		(38,745)
Pension liability		(33,865)	(2,431)		(36,296)
	\$ 539,196	\$ 571,532	\$ 231,934	\$ (591,092)	\$ 751,570

**Table of Contents**

## CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS

FOR THE SIX MONTHS

ENDED JULY 1, 2012

	GUARANTOR SUBSIDIARIES	NON- GUARANTOR SUBSIDIARIES	INTERFACE, INC. (PARENT CORPORATION) (In thousands)	CONSOLIDATION AND ELIMINATION ENTRIES	CONSOLIDATED TOTALS
Net cash provided by operating activities	\$ 6,532	\$ 2,812	\$ 10,667	\$ 3,418	\$ 23,429
Cash flows from investing activities:					
Purchase of plant and equipment	(7,292)	(14,443)	(12)		(21,747)
Other	390	(31)	(1,496)		(1,137)
Net cash used for investing activities	(6,902)	(14,474)	(1,508)		(22,884)
Cash flows from financing activities:					
Repurchase of senior subordinated notes			(11,477)		(11,477)
Other	715	2,536	167	(3,418)	
Proceeds from issuance of common stock			131		131
Dividends paid			(2,627)		(2,627)
Net cash provided by (used for) financing activities	715	2,536	(13,806)	(3,418)	(13,973)
Effect of exchange rate change on cash		(329)			(329)
Net increase (decrease) in cash	345	(9,455)	(4,647)		(13,757)
Cash at beginning of period	1,101	35,874	13,660		50,635
Cash at end of period	\$ 1,446	\$ 26,419	\$ 9,013	\$	\$ 36,878

---

**Table of Contents**

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

Our discussions below in this Item 2 are based upon the more detailed discussions about our business, operations and financial condition included in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012, under Item 7 of that Form 10-K. Our discussions here focus on our results during the quarter and six months ended, or as of, July 1, 2012, and the comparable periods of 2011 for comparison purposes, and, to the extent applicable, any material changes from the information discussed in that Form 10-K or other important intervening developments or information since that time. These discussions should be read in conjunction with that Form 10-K for more detailed and background information.

Forward-Looking Statements

This report contains statements which may constitute forward-looking statements within the meaning of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended by the Private Securities Litigation Reform Act of 1995. 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 under the heading Risk Factors included in Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended January 1, 2012, which discussion is hereby incorporated by reference. The Company undertakes 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.

2012 Restructuring Charge

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 consists 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. The charge is comprised of employee severance expenses of \$5.4 million, other related exit costs of \$1.6 million, and a charge for impairment of assets of approximately \$9.3 million. Approximately \$7 million of the charge will result in cash expenditures, primarily severance expense. The restructuring plan was substantially completed in the second quarter of 2012, and is expected to yield annualized cost savings of approximately \$9 million.

2011 Restructuring Charge

In the fourth quarter of 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 \$6.2 million in the fourth quarter of 2011. The majority of this charge (\$5.4 million) relates to the severance of approximately 110 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 \$5.4 million of this charge will result in cash expenditures, primarily severance expenses. Actions and expenses related to this plan were substantially completed by the end of 2011.

Discontinued Operations

In 2007, we sold our Fabrics Group business segment. In accordance with applicable accounting standards, we have reported the results of operations for the former Fabrics Group business segment as discontinued operations, where applicable.

Our discontinued operations had no net sales and no net income or loss in either of the three-month or six-month periods ended July 1, 2012 and July 3, 2011.

Recent Events

In July 2012, a fire occurred at the Company's facility in Picton, Australia, and the Company entered into an agreement to sell its Bentley Prince Street business segment. Please see Notes 14 and 15 in the notes to consolidated financial statements in Item 1 of this Quarterly Report on Form 10-Q.

**Table of Contents**

## General

During the quarter ended July 1, 2012, we had net sales of \$254.6 million, compared with net sales of \$267.6 million in the second quarter last year. Fluctuations in currency exchange rates negatively impacted 2012 second quarter sales by 3% (approximately \$7 million), compared with the prior year period. During the first six months of fiscal year 2012, we had net sales of \$487.4 million, compared with net sales of \$513.0 million in the first six months of last year. Fluctuations in currency exchange rates negatively impacted sales in the first six months of 2012 by 2% (approximately \$10 million), compared with the prior year period.

Included in our results for the six months ended July 1, 2012 is a restructuring charge of \$16.3 million, as described above.

During the second quarter of 2012, we had net income of \$10.3 million, or \$0.16 per diluted share, compared with net income of \$12.8 million, or \$0.20 per diluted share, in the second quarter of 2011. During the six months ended July 1, 2012, including the \$16.3 million restructuring charge described above, we had net income of \$4.3 million, or \$0.07 per diluted share, compared with net income of \$22.6 million, or \$0.35 per diluted share, in the first six months of 2011.

## Results of Operations

The following table presents, as a percentage of net sales, certain items included in our Consolidated Condensed Statements of Operations for the three-month and six-month periods ended July 1, 2012, and July 3, 2011, respectively:

	Three Months Ended		Six Months Ended	
	July 1, 2012	July 3, 2011	July 1, 2012	July 3, 2011
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	66.8	64.6	67.0	64.6
Gross profit on sales	33.2	35.4	33.0	35.4
Selling, general and administrative expenses	24.6	25.6	25.0	26.1
Restructuring and asset impairment charge			3.3	
Operating income	8.7	9.8	4.6	9.3
Interest/Other expenses	2.5	2.6	2.8	2.6
Income before tax expense	6.1	7.2	1.9	6.7
Income tax expense	2.1	2.4	1.0	2.2
Net income	4.0	4.8	0.9	4.4

Below we provide information regarding net sales for each of our operating segments, and analyze those results for the three-month and six-month periods ended July 1, 2012, and July 3, 2011, respectively.

*Net Sales by Business Segment*

Net sales by operating segment and for our Company as a whole were as follows for the three-month and six-month periods ended July 1, 2012, and July 3, 2011, respectively:

Net Sales By Segment	Three Months Ended		Percentage Change
	July 1, 2012	July 3, 2011	
	(In thousands)		
Modular Carpet	\$ 229,546	\$ 240,566	(4.6)%
Bentley Prince Street	25,061	27,074	(7.4)%

Edgar Filing: INTERFACE INC - Form 10-Q

Total	\$ 254,607	\$ 267,640	(4.9)%
-------	------------	------------	--------

-21-

**Table of Contents**

Net Sales By Segment	Six Months Ended		Percentage Change
	July 1, 2012	July 3, 2011	
	(In thousands)		
Modular Carpet	\$ 439,562	\$ 459,846	(4.4)%
Bentley Prince Street	47,805	53,196	(10.1)%
<b>Total</b>	<b>\$ 487,367</b>	<b>\$ 513,042</b>	<b>(5.0)%</b>

*Modular Carpet Segment.* For the quarter ended July 1, 2012, net sales for the Modular Carpet segment declined \$11.0 million (4.6%) versus the comparable period in the prior year. On a geographic basis, sales increases in the Americas (up 6%) were offset by declines in the Europe (down 13% in U.S. dollars and 2% in local currencies) and Asia-Pacific (down 18%) regions. Sales growth in the Americas was due to increases in both the corporate office market (up 5%) and non-office markets. The strongest performing non-office market segments were residential (up 18%), retail (up 15%) and education (up 13%). The increase in the residential segment was due to new FLOR store openings as well as same store growth. These increases in the Americas were somewhat offset by declines in the government (down 25%) and healthcare (down 4%) market segments. In Europe, the sales decline was due primarily to negative currency translation impacts, as most market segments were flat in local currencies, with the exception of the retail (down 25% in local currencies and 33% in U.S. dollars) and government (down 10% in local currencies and 20% in U.S. dollars) market segments. Asia-Pacific, in the face of strong prior year comparable sales in the second quarter, saw declines in almost all market segments, with education (down 55%) showing the most significant decline due to the curtailment of government stimulus programs that had been in place in 2011 particularly in Australia.

For the six months ended July 1, 2012, net sales for the Modular Carpet segment declined \$20.3 million (4.4%) versus the comparable period in the prior year. On a geographic basis, we experienced increases in the Americas (up 3%) offset by declines in Europe (down 2% in local currencies and 8% in U.S. dollars) and Asia-Pacific (down 17%). In the Americas, the residential market segment made the largest gain (up 34%), particularly due to the opening of seven FLOR retail stores compared with the number of stores at the end of the second quarter of 2011. The education (up 9%), retail (up 6%) and corporate office (up 3%) market segments also experienced increases during the period. These gains were somewhat offset by a decline in the government market segment (down 22%) during the first six months of 2012 versus the prior year period. In Europe, all market segments declined as reported in U.S. dollars for the six months ended July 2, 2012, versus the comparable period in 2011, due to adverse currency translation impacts. However, in local currencies, the corporate office market segment in Europe experienced an increase of 4%. Asia-Pacific saw the largest decline in the education segment (down 59%), primarily as a result of the curtailment of government stimulus programs that had been in place in 2011 particularly in Australia. The corporate office (down 6%) and hospitality (down 45%) market segments also experienced declines in Asia-Pacific compared with the first six months of 2012.

*Bentley Prince Street Segment.* In our Bentley Prince Street segment, net sales for the quarter ended July 1, 2012 declined \$2.0 million (7.4%) versus the comparable period in 2011. The primary driver of the decrease in sales was the decline in the corporate office market segment (down 21%). This decrease was partially offset by increases in the government (up 58%) and hospitality (up over 100%) market segments.

For the six months ended July 1, 2012, net sales for the Bentley Prince Street segment declined \$5.4 million (10.1%) versus the comparable period in 2011. The decrease was primarily attributable to the corporate office market segment (down 17%) as well as a decline in the government market segment (down 4%). These declines were partially mitigated by increases in the healthcare (up 22%) and hospitality (up 13%) market segments.

**Table of Contents***Cost and Expenses*

*Company Consolidated.* The following table presents, on a consolidated basis for our operations, our overall cost of sales and selling, general and administrative expenses for the three-month and six-month periods ended July 1, 2012, and July 3, 2011, respectively:

Cost and Expenses	Three Months Ended		Percentage Change
	July 1, 2012	July 3, 2011	
	(In thousands)		
Cost of sales	\$ 170,012	\$ 172,865	(1.7)%
Selling, general and administrative expenses	62,562	68,638	(8.9)%
<b>Total</b>	<b>\$ 232,574</b>	<b>\$ 241,503</b>	<b>(3.7)%</b>

Cost and Expenses	Six Months Ended		Percentage Change
	July 1, 2012	July 3, 2011	
	(In thousands)		
Cost of sales	\$ 326,569	\$ 331,339	(1.4)%
Selling, general and administrative expenses	121,930	134,038	(9.0)%
<b>Total</b>	<b>\$ 448,499</b>	<b>\$ 465,377</b>	<b>(3.6)%</b>

For the quarter ended July 1, 2012, our cost of sales decreased \$2.9 million (1.7%) versus the comparable period in the prior year. Almost all of the decrease was attributable to fluctuations in currency rates in the second quarter of 2012 versus the second quarter of 2011. Our raw materials prices in the second quarter of 2012 were approximately 1-2% higher than in the comparable period of 2012. Due to lower absorption of fixed costs associated with lower production volumes, as a percentage of sales, cost of sales increased to 66.8% for the three months ended July 1, 2012, versus 64.6% in the comparable prior year period. On a sequential basis versus the first quarter of 2012, we saw an improvement in cost of sales as a percentage of sales. We believe that as the savings related to our first quarter 2012 restructuring plan are fully realized in the later part of 2012, cost of sales will further decrease as a percentage of sales.

For the six months ended July 1, 2012, cost of sales decreased \$4.8 million (1.4%) versus the comparable period in the prior year. Currency fluctuation accounted for the majority of the decline versus the 2011 period. Our raw materials prices were approximately 2-3% higher for the first six months of 2012 versus the first six months of 2011. Due to this cost increase, coupled with lower absorption of fixed costs associated with lower production volumes, cost of sales as a percentage of sales increased to 67.0% for the 2012 period versus 64.6% for the 2011 period. As noted above, we believe that as the savings related to our first quarter 2012 restructuring plan are fully realized in the later part of 2012, cost of sales will further decrease as a percentage of sales.

For the quarter ended July 1, 2012, our selling, general and administrative expense decreased \$6.1 million (8.9%) versus the comparable period in 2011. Fluctuations in currency exchange rates accounted for approximately \$2 million of this decrease. The primary component of the decrease in selling, general and administrative expenses was lower selling and marketing expenses of approximately \$3.0 million. This decrease was primarily due to the realization of savings from our restructuring plans which were put in place in late 2011 and early 2012, as well as lower selling costs associated with lower sales volume in the second quarter of 2012 versus the comparable period in 2011. Administrative expenses also declined approximately \$2.0 million in the period versus the prior year, also a result of our restructuring programs. Due to these items, as a percentage of sales our selling, general and administrative expenses decreased to 24.6% for the second quarter of 2012 versus 25.6% for the second quarter of 2011.

For the six months ended July 1, 2012, our selling, general and administrative expenses decreased \$12.1 million (9.0%) versus the comparable period in the prior year. As noted above, this decrease was largely due to the impact of our restructuring plans put in place in late 2011 and early 2012. Selling and marketing expenses decreased by approximately \$3.0 million during the first six months of 2012 versus 2011 due to the savings from these plans, although this decrease was slightly offset by increased marketing costs due to trade show and similar expenses, primarily in the first three months of 2012. Administrative expenses declined by approximately \$8.0 million during the 2012 six-month period, due to savings from our restructuring plans, as well as lower levels of non-cash incentive compensation in the first six months of 2012 versus 2011.





**Table of Contents**

*Cost and Expenses by Segment.* The following table presents the combined cost of sales and selling, general and administrative expenses for each of our operating segments:

Cost of Sales and Selling, General and Administrative Expenses (Combined)	Three Months Ended		Percentage Change
	July 1, 2012	July 3, 2011	
	(In thousands)		
Modular Carpet	\$ 205,512	\$ 213,630	(3.8)%
Bentley Prince Street	26,293	26,978	(2.5)%
Corporate Expenses and Eliminations	769	895	(14.1)%
Total	\$ 232,574	\$ 241,503	(3.7)%
	(In thousands)		
	Six Months Ended		Percentage Change
	July 1, 2012	July 3, 2011	
Modular Carpet	\$ 398,129	\$ 407,025	(2.2)%
Bentley Prince Street	49,601	53,257	(6.9)%
Corporate Expenses and Eliminations	769	5,095	(84.9)%
Total	\$ 448,499	\$ 465,377	(3.6)%

*Interest Expense*

For the three-month period ended July 1, 2012, our interest expense decreased \$0.7 million to \$6.1 million, versus \$6.8 million in the comparable period of 2011. The primary reason for this decrease was the redemption of the remaining \$11.5 million of our 9.5% Senior Subordinated Notes early in the second quarter of 2012, leading to lower interest expense for the balance of the quarter. The decrease was also due in part to lower amounts of bank fees for the second quarter of 2012 versus 2011. For the six months ended July 1, 2012, our interest expense decreased by approximately \$0.6 million to \$12.8 million, versus \$13.4 million in the comparable period of 2011. This decrease was due to the same factors described for the three-month period ended July 1, 2012.

*Liquidity and Capital Resources**General*

At July 1, 2012, we had \$36.9 million in cash. At that date, 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 July 1, 2012, we could have incurred \$84.3 million of additional borrowings under our domestic revolving credit facility and 20.0 million (approximately \$24.9 million) of additional borrowings under our European credit facility. In addition, we could have incurred an additional \$18.5 million of borrowings under our other credit facilities in place at other non-U.S. subsidiaries.

*Analysis of Cash Flows*

Our primary sources of cash during the six months ended July 1, 2012 were (1) \$14.8 million due to a reduction in accounts receivable, and (2) \$4.0 million due to an increase in accounts payable and accrued expenses. Our primary uses of cash during this period were (1) \$21.7 million for capital expenditures, (2) \$11.5 million for the redemption of our remaining 9.5% Senior Subordinated Notes, and (3) \$9.6 million for increased inventory levels.

---

**Table of Contents**

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

Our discussion below in this Item 3 is based upon the more detailed discussions of our market risk and related matters included in our Annual Report on Form 10-K for the fiscal year ended January 1, 2012, under Item 7A of that Form 10-K. Our discussion here focuses on the period ended July 1, 2012, and any material changes from (or other important intervening developments since the time of) the information discussed in that Form 10-K. This discussion should be read in conjunction with that Form 10-K for more detailed and background information.

At July 1, 2012, we recognized a \$4.9 million decrease in our foreign currency translation adjustment account compared to January 1, 2012, primarily because of the strengthening of the U.S. dollar against certain foreign currencies, particularly the Euro.

*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 July 1, 2012. The values that result from these computations are compared with the market values of these financial instruments at July 1, 2012. The differences in this comparison are the hypothetical gains or losses associated with each type of risk.

As of July 1, 2012, based on a hypothetical immediate 150 basis point increase in interest rates, with all other variables held constant, the market value of our fixed rate long-term debt would be impacted by a net decrease of approximately \$15.8 million. Conversely, a 150 basis point decrease in interest rates would result in a net increase in the market value of our fixed rate long-term debt of approximately \$6.4 million.

As of July 1, 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 financial instruments of \$8.4 million or an increase in the fair value of our financial instruments of \$6.8 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 4. CONTROLS AND PROCEDURES**

As of the end of the period covered by this Quarterly Report on Form 10-Q, an evaluation was performed under the supervision and with the participation of our management, including our President and Chief Executive Officer and our Senior Vice President and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the Act), pursuant to Rule 13a-14(c) under the Act. Based on that evaluation, our President and Chief Executive Officer and our Senior Vice President and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report.

There were no changes in our internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents**

PART II - OTHER INFORMATION

ITEM 1. 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 1.

ITEM 1A. RISK FACTORS

The specific risk factor under the heading "The estate of our former Chairman currently has sufficient voting power to elect a majority of our Board of Directors," set forth in Part I, Item 1A in our Annual Report on Form 10-K for fiscal year 2011, is no longer applicable. For a discussion of risk factors, see that Item in our 2011 Form 10-K.

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

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

The following exhibits are filed with this report:

EXHIBIT

NUMBER	DESCRIPTION OF EXHIBIT
31.1	Section 302 Certification of Chief Executive Officer.
31.2	Section 302 Certification of Chief Financial Officer.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. § 1350.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. § 1350.
101.INS	XBRL Instance Document (furnished electronically herewith)*
101.SCH	XBRL Taxonomy Extension Schema Document (furnished electronically herewith)*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document (furnished electronically herewith)*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document (furnished electronically herewith)*
101.PRE	XBRL Taxonomy Presentation Linkbase Document (furnished electronically herewith)*
101.DEF	XBRL Taxonomy Definition Linkbase Document (furnished electronically herewith)*

Edgar Filing: INTERFACE INC - Form 10-Q

\* In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed to be furnished and not filed .

**Table of Contents**

SIGNATURE

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

INTERFACE, INC.

Date: August 9, 2012

By: /s/ Patrick C. Lynch  
Patrick C. Lynch  
Senior Vice President  
(Principal Financial Officer)

-27-

**Table of Contents**

EXHIBIT INDEX

EXHIBIT

NUMBER	DESCRIPTION OF EXHIBIT
31.1	Section 302 Certification of Chief Executive Officer
31.2	Section 302 Certification of Chief Financial Officer
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. § 1350
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. § 1350
101.INS	XBRL Instance Document (furnished electronically herewith)*
101.SCH	XBRL Taxonomy Extension Schema Document (furnished electronically herewith)*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document (furnished electronically herewith)*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document (furnished electronically herewith)*
101.PRE	XBRL Taxonomy Presentation Linkbase Document (furnished electronically herewith)*
101.DEF	XBRL Taxonomy Definition Linkbase Document (furnished electronically herewith)*

\* In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed to be furnished and not filed .