TCP Capital Corp.
Form N-2/A
December 05, 2013

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As filed with the Securities and Exchange Commission on December 4, 2013

Securities Act Registration No. 333-192066

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-2

ý Registration Statement under the Securities Act of 1933
ý Pre-Effective Amendment No. 1
o Post-Effective Amendment No.
and/or
o Registration Statement Under the Investment Company Act of 1940
o Amendment No.

TCP CAPITAL CORP.

(Exact Name of Registrant as Specified in its Charter)

2951 28th Street, Suite 1000
Santa Monica, California 90405

(Address of Principal Executive Offices)

(310) 566-1094

(Registrant's Telephone Number, Including Area Code)

Howard M. Levkowitz
Tennenbaum Capital Partners, LLC
2951 28th Street, Suite 1000
Santa Monica, California 90405

(Name and Address of Agent for Service)

Copies to:

Richard T. Prins, Esq.
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Skadden, Arps, Slate, Meagher & Flom LLP
Four Times Square
New York, New York 10036
212-735-3000

Approximate Date of Proposed Public Offering:

From time to time after the effective date of this Registration Statement.

If any securities being registered on this form will be offered on a delayed or continuous basis in reliance on Rule 415 under the Securities Act of 1933, other than securities offered in connection with a distribution reinvestment plan, check the following box. ý

It is proposed that this filing will become effective (check appropriate box):

o when declared effective pursuant to section 8(c).
If appropriate, check the following box:

o This post-effective amendment designates a new effective date for a previously filed post-effective amendment registration statement.

o This form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act and the Securities Act registration statement number of the earlier effective registration statement for the same offering is __________________.

CALCULATION OF REGISTRATION FEE UNDER THE SECURITIES ACT OF 1933

Title of Securities Being Registered	Amount Being Registered	Proposed Maximum Offering Price per Unit	Proposed Maximum Aggregate Offering Price(1)(2)	Amount of Registration Fee(4)
Common Stock, par value $0.001 per share	N/A	N/A	$250,000,000(3)	$32,202

(1) Includes underwriters' option to purchase additional shares.

(2) Estimated pursuant to Rule 457(o) under the Securities Act of 1933 (the "Securities Act") solely for the purpose of determining the registration fee.

(3) In no event shall the aggregate offering price of all securities issued from time to time pursuant to the registration statement exceed $250,000,000.

(4) $243,550 aggregate principal amount of securities remain registered and unsold pursuant to Registration Statement No. 333-185319 (initially filed by the Registrant on December 7, 2012), which represents a filing fee previously paid by the Registrant of $33.22 for the unsold securities. Pursuant to Rule 415(a)(6) of the Securities Act, the $33.22 filing fee previously paid by the Registrant for the unsold securities under Registration Statement No. 333-185319 offsets a portion of the $32,202 fees due for this Registration Statement. The remaining registration fee amount was previously paid.

Special Value Continuation Partners, LP has also signed the registrant's registration statement.

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

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Subject To Completion, Preliminary Prospectus dated December 4, 2013

The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the Registration Statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

P R O S P E C TU S **$250,000,000**

Common Stock

We are a holding company (the "Holding Company") with no direct operations of our own, and currently our only business and sole asset is our ownership of all of the common limited partner interests in Special Value Continuation Partners, LP (the "Operating Company"), which represents approximately 100% of the common equity and 74.8% of the combined common and preferred equity interests of the Operating Company as of September 30, 2013. We and the Operating Company are externally managed, closed-end, non-diversified management investment companies that have elected to be treated as business development companies under the Investment Company Act of 1940 (the "1940 Act"). Our and the Operating Company's investment objective is to achieve high total returns through current income and capital appreciation, with an emphasis on principal protection. Both we and the Operating Company seek to achieve this investment objective primarily through investments in debt securities of middle-market companies. Our primary investment focus is investing in and originating leveraged loans to performing middle-market companies.

Tennenbaum Capital Partners, LLC (the "Advisor") serves as our and the Operating Company's investment advisor. The Advisor is a leading investment manager and specialty lender to middle-market companies that had in excess of $5.0 billion in capital commitments from investors ("committed capital") under management as of September 30, 2013, approximately 15% of which consists of our committed capital. SVOF/MM, LLC, an affiliate of the Advisor, is the Operating Company's general partner and provides the administrative services necessary for us to operate.

We may offer, from time to time, in one or more offerings or series, together or separately, up to $250 million in shares of our common stock to provide us with additional capital. Shares of our common stock may be offered at prices and on terms to be disclosed in one or more supplements to this prospectus. You should read this prospectus and the applicable prospectus supplement carefully before you invest in shares of our common stock.

We may offer shares of common stock at a discount to net asset value per share in certain circumstances. Sales of common stock at prices below net asset value per share dilute the interests of existing stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share. At our 2013 annual meeting, held on May 1, 2013, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering, our stockholders approved our ability to sell or otherwise issue shares of our common stock at any level of discount from net asset value per share for a twelve month period expiring on the anniversary of the date of stockholder approval.

Shares of our common stock may be offered directly to one or more purchasers, or through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to a particular offering will identify any agents, underwriters or dealers involved in the sale of shares of our common stock, and will disclose any applicable purchase price, fee, commission or discount arrangement between us and our agents, underwriters or dealers, or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell any shares of our common stock through agents, underwriters or dealers without delivery of the prospectus and a prospectus supplement describing the method and terms of the offering of such shares of common stock. Our common stock is traded on The NASDAQ Global Select Market under the symbol "TCPC." As of December 3, 2013, the last reported sales price for our common stock was $16.87. The net asset value per share of our common stock at September 30, 2013 (the last date prior to the date of this prospectus on which we determined net asset value) was $15.06.

This prospectus contains important information you should know before investing in our common stock. Please read it carefully before you invest and keep it for future reference. We file annual, quarterly and current reports, proxy statements and other information about us with the Securities and Exchange Commission. A Statement of Additional Information, dated , 2013, containing additional information about the Holding Company and the Operating Company has been filed with the Securities and Exchange Commission (the "SEC") and is incorporated by reference in its entirety into this prospectus. The Advisor maintains a website at http://www.tennenbaumcapital.com and we make all of our annual, quarterly and current reports, proxy statements and other publicly filed information available, free of charge, on or through this website. You may also obtain free copies of our annual and quarterly reports, request a free copy of the Statement of Additional Information, the table of contents of which is on page 137 of this prospectus and make stockholder inquiries by contacting us at Tennenbaum Capital Partners, LLC, c/o Investor Relations, 2951 28th Street, Suite 1000, Santa Monica, California 90405 or by calling us collect at (310) 566-1094. The SEC maintains a website at http://www.sec.gov where such information is available without charge upon request. Information contained on our website is not incorporated by reference into this prospectus, and you should not consider information contained on our website to be part of this prospectus.

The debt securities in which we typically invest are either rated below investment grade by independent rating agencies or would be rated below investment grade if such securities were rated by rating agencies. Below investment grade securities, which are often referred to as "hybrid securities," "junk bonds" or "leveraged loans" are regarded as having predominantly speculative characteristics with respect to the issuer's capacity to pay interest and repay principal. They may be illiquid and difficult to value and typically do not require repayment of principal prior to maturity, which potentially heightens the risk that we may lose all or part of our investment. In addition, a majority of the Operating Company's debt investments include interest reset provisions that may make it more difficult for the borrowers to make debt repayments to the Operating Company if the reset provision has the effect of increasing the applicable interest rate.

Shares of closed-end investment companies, including business development companies, frequently trade at a discount from their net asset value. If our shares trade at a discount to our net asset value, it will likely increase the risk of loss for purchasers in the offerings. Investing in our common stock involves a high degree of risk, including credit risk and the risk of the use of leverage. Before buying any shares of our common stock, you should read the discussion of the material risks of investing in our common stock in "Risks" beginning on page 23 of this prospectus.

Neither the SEC nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

This prospectus may not be used to consummate sales of shares of our common stock unless accompanied by a prospectus supplement.

The date of this prospectus is , 2013.

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Statistical and market data used in this prospectus has been obtained from governmental and independent industry sources and publications. We have not independently verified the data obtained from these sources. Forward-looking information obtained from these sources is subject to the same qualifications and the additional uncertainties regarding the other forward-looking statements contained in this prospectus, for which the safe harbor provided in Section 27A of the Securities Act and Section 21E of the Securities Exchange Act is not available.

You should rely only on the information contained in this prospectus, the Statement of Additional Information, or SAI, incorporated by reference in its entirety in this prospectus, and the accompanying prospectus supplement. We have not, and the underwriters have not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and no underwriters are, making offers to sell these securities in any jurisdiction where such offer or sale is not permitted. You should assume that the information in this prospectus is accurate only as of the date on the front of this prospectus, the information in the SAI is accurate only as of its respective date and the information in the accompanying prospectus supplement is accurate only as of the date on the front of the accompanying prospectus supplement. Our business, financial condition and prospects may have changed since that date. To the extent required by applicable law, we will update this prospectus and the SAI during the offering period to reflect material changes to the disclosure herein.

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ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we have filed with the SEC, using the "shelf" registration process. Under the shelf registration process, we may offer, from time to time on a delayed basis over a three year period, up to $250 million in shares of our common stock. The shares of our common stock may be offered at prices and on terms described in one or more supplements to this prospectus. This prospectus provides you with a general description of the shares of our common stock that we may offer. Each time we use this prospectus to offer shares of our common stock, we will provide a prospectus supplement that will contain specific information about the terms of that offering. The prospectus supplement may also add, update or change information contained in this prospectus. Please carefully read this prospectus and any prospectus supplement together with any exhibits and the additional information described under the heading "Additional Information" and the section under the heading "Risks" before you make an investment decision.

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PROSPECTUS SUMMARY

This summary highlights some of the information in this prospectus. This summary is not complete and may not contain all of the information that you may want to consider before investing in our common stock. You should read the entire prospectus, including "Risks," and the Statement of Additional Information, dated , 2013 (the "SAI").

Throughout this prospectus, unless the context otherwise requires, a reference to:

"*Holding Company" refers to Special Value Continuation Fund, LLC, a Delaware limited liability company, for the periods prior to the consummation of the Conversion (as defined below) described elsewhere in this prospectus and to TCP Capital Corp. for the periods after the consummation of the Conversion;*

"*Operating Company" refers to Special Value Continuation Partners, LP, a Delaware limited partnership;*

"TCPC Funding" refers to TCPC Funding I LLC, a Delaware limited liability company;

"*Advisor" refers to Tennenbaum Capital Partners, LLC, a Delaware limited liability company and the investment manager; and*

"*General Partner" and "Administrator" refer to SVOF/MM, LLC, a Delaware limited liability company, the general partner of the Operating Company and an affiliate of the Advisor and administrator of the Holding Company and the Operating Company.*

For simplicity, this prospectus uses the term "Company," "we," "us" and "our" to include the Holding Company and, where appropriate in the context, the Operating Company and TCPC Funding, on a consolidated basis. For example, (i) although all or substantially all of the net proceeds from the offerings will be invested in the Operating Company and all or substantially all of the Holding Company's investments will be made through the Operating Company, this prospectus generally refers to the Holding Company's investments through the Operating Company as investments by the "Company," and (ii) although the Operating Company and TCPC Funding and not the Holding Company has entered into the Leverage Program (defined below), this prospectus generally refers to the Operating Company's use of the Leverage Program as borrowings by the "Company," in all instances in order to make the operations and investment strategy easier to understand. The Holding Company and the Operating Company have the same investment objective and policies and the assets, liabilities and results of operations of the Holding Company are consolidated with those of the Operating Company as described below under " Operating and Regulatory Tax Structure."

On April 2, 2012, we completed a conversion under which TCP Capital Corp. succeeded to the business of Special Value Continuation Fund, LLC and its consolidated subsidiaries, and the members of Special Value Continuation Fund, LLC became stockholders of TCP Capital Corp. In this prospectus, we refer to such transactions as the "Conversion." Unless otherwise indicated, the disclosure in this prospectus gives effect to the Conversion.

The Company

We are an externally managed, non-diversified closed-end management investment company that has elected to be regulated as a business development company, or BDC, under the Investment Company Act of 1940, as amended, or the 1940 Act. See " Company History and BDC Conversion." We completed our initial public offering on April 10, 2012. Our investment objective is to achieve high total returns through current income and capital appreciation, with an emphasis on principal protection. We seek to achieve our investment objective primarily through investments in debt securities of middle-market companies, which we typically define as those with enterprise values between $100 million and $1.5 billion. While we primarily focus on privately negotiated investments in debt of middle-market companies, we make investments of all kinds and at all levels of the capital structure, including in equity interests such as preferred or common stock and warrants or options received in connection with our debt investments. Our investment activities benefit from what we believe are the competitive advantages of the Advisor, including its diverse in-house skills, proprietary deal flow, and consistent and rigorous investment process focused on established, middle-market companies. We expect to generate returns through a combination of the receipt of contractual interest payments on debt investments and origination and similar fees, and, to a lesser extent, equity appreciation through options, warrants, conversion rights or direct equity investments. Substantially all of our operating history and performance results have been achieved through our predecessor, Special Value Continuation Fund, LLC, which was a registered investment company but was neither a business development company nor a publicly traded company. There are no material operating differences between us and our predecessor, however, as a BDC we are deemphasizing distressed debt investments, which may adversely affect our investment returns. See " Company History and BDC Conversion."

As described in more detail below under " Company History and BDC Conversion," we have no employees of our own and currently our only business and sole asset is the ownership of all of the common limited partner interests of the Operating Company. Our investment activities are externally managed by the Advisor, a leading investment manager with in excess of $5.0 billion in capital commitments from investors ("committed capital") under management, approximately 15% of which consists of the Holding Company's committed capital under management as of September 30, 2013, and a primary focus on providing financing to middle-market companies. Additionally, the Holding Company expects that it will continue to seek to qualify as a regulated investment company, or RIC, under Subchapter M of the Internal Revenue Code, or the Code.

Investment Portfolio

At December 31, 2012, our existing investment portfolio consisted of debt and equity positions in 54 portfolio companies valued at approximately $517.7 million. Debt positions represented approximately 93% of the total portfolio fair value and had a weighted-average effective yield and yield to maturity of approximately 11.3% and 11.6%, respectively. For purposes of this prospectus, references to "yield to maturity" assume that debt investments in our portfolio as of a certain date are purchased at fair value on that date and held until their respective maturities with no prepayments or losses and are exited at par upon maturity. At December 31, 2012, the weighted-average remaining term of our debt investments was approximately 4.7 years. At December 31, 2012, the average investment size in our existing portfolio by issuer was $9.6 million. As of December 31, 2012, approximately 7.9% of our total assets consisted of distressed debt investments, none of which were delinquent, non-performing or in default. Equity positions represented approximately 7% of the total fair value of our investment portfolio. See " Investment Strategy" for more information.

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The following charts summarize our portfolio mix by industry and type based on the fair value of our investments as of December 31, 2012.

Investment by Industry **Investment by Asset Type**

Tennenbaum Capital Partners, LLC

Our investment activities are managed by the Advisor. The Advisor is a leading investment manager (including specialty lending to middle-market companies). The Advisor is a Delaware limited liability company and is registered as an investment advisor under the Investment Advisers Act of 1940, or the Advisers Act. As of September 30, 2013, the Advisor had in excess of $5.0 billion in committed capital under management, approximately 15% of which consists of the Holding Company's committed capital, and a team of approximately 30 investment professionals supported by approximately 45 administrative and back office personnel that focus on operations, finance, legal and compliance, accounting and reporting, investor relations, and information technology. The Advisor was founded in 1999 by Michael E. Tennenbaum, Mark K. Holdsworth and Howard M. Levkowitz, and its predecessor entity formed and commenced operations in 1996. The three founders along with David A. Hollander, Michael E. Leitner, Philip M. Tseng and Rajneesh Vig constitute the Advisor's active partners, or the Advisor Partners. The Advisor Partners have significant industry experience, including experience investing in middle-market companies. Together, the Advisor Partners have invested approximately $12.6 billion in over 300 companies since the Advisor's inception, through multiple business and credit cycles, across all segments of the capital structure through a broad set of credit-oriented strategies including leveraged loan origination, secondary investments of discounted debt securities, and distressed and control opportunities. We refer to the products that employ these strategies within the Advisor's platform as the Opportunity Funds. We believe the Advisor Partners' investment perspectives, complementary skills, and collective investment experience provides the Advisor with a strategic and competitive advantage in middle-market investing.

As our investment advisor, the Advisor is responsible for sourcing potential investments, conducting research, analyzing investment opportunities and structuring our investments and monitoring our portfolio companies on an ongoing basis. We believe that the Advisor has a proven long-term track record of positive performance, notwithstanding some periods during which losses were incurred, of sourcing deals, originating loans and successfully investing in middle-market companies and that the relationships of its investment professionals are integral to the Advisor's success. The Advisor's investment professionals have long-term working relationships with key sources of investment opportunities and industry expertise, including investment bankers, financial advisors, attorneys, private equity sponsors, other senior lenders, high-yield bond specialists, research analysts, accountants, and senior management teams. Additionally, the Advisor's structure includes both a board of advisors and a group of Senior Executive Advisors, a team comprised of approximately 20 current and former executives from a variety of industries, which extends the reach of the Advisor's relationships through a group of seasoned industry leaders and that can enhance our deal sourcing and due diligence activities.

We also benefit from the existing infrastructure and administrative capabilities of an established investment manager. The General Partner, an affiliate of the Advisor, serves as our Administrator and provides us with office space, equipment and office services. The tasks of our Administrator include overseeing our financial records, preparing reports to our stockholders and reports filed with the Securities and Exchange Commission (the "SEC") and generally monitoring the payment of our expenses and the performance of administrative and professional services rendered to us by others.

Since the beginning of 2011, the Advisor executed over $1.75 billion in direct origination leveraged loans primarily to middle-market companies, of which over $634 million was for our account. There can be no assurance that similar deal flow or terms will be available in the future for loans in which we may invest.

Investment Strategy

To achieve our investment objectives, we intend to focus on a subset of the broader investment strategies historically pursued by the Advisor. Our primary investment focus is the ongoing origination of and investments in leveraged loans of performing middle-market companies, building on the Advisor's established track record of origination and participation in the original syndication of approximately $5.1 billion of leveraged loans to 125 companies since 1999, of which we invested over $1.1 billion in 76 companies. For the purposes of this prospectus, the term "leveraged loans" refers to senior debt investments that rank ahead of subordinated debt and that generally have the benefit of security interests in the assets of the borrower.

Our investments generally range from $10 million to $35 million per company, the size of which may grow over time in proportion with our capital base. We expect to generate current returns through a combination of the receipt of contractual interest payments on debt investments and origination and similar fees, and, to a lesser extent, equity appreciation through options, warrants, conversion rights or direct equity investments. We often receive equity interests such as preferred or common stock and warrants or options in connection with our debt investments. From time to time we may also use other investment strategies, which are not our primary focus, to attempt to enhance the overall return of our portfolio. These investment strategies may include, but are not limited to, the purchase of discounted debt, opportunistic investments, and financial instruments to hedge currency or interest rate risk associated with our portfolio.

Our typical investments are in performing middle-market companies. We believe that middle-market companies are generally less able to secure financing than larger companies and thus offer better return opportunities for those able to conduct the necessary diligence to appropriately evaluate these companies. We focus primarily on U.S. companies where we believe the Advisor's perspective, complementary skills and investment experience provides us with a competitive advantage and in industries where the Advisor sees an attractive risk reward profile due to macroeconomic trends and the Advisor's existing industry expertise.

Our Competitive Advantages

We believe that we possess the following competitive advantages over other capital providers to middle-market companies:

Focus on minimizing the risk of loss and achieving attractive risk-adjusted returns. We primarily structure investments to attempt to achieve high cash yields, cash origination fees, conservative leverage, and strong contractual protections that reduce the risk of principal loss. Contractual protections may include default premiums, information rights, board governance rights, and affirmative, negative and financial covenants, such as lien protection and prohibitions against change of control. While we do not expect to undertake a material focus on distressed investments, we believe that the Advisor's experience in distressed investing from managing other funds helps us negotiate more favorable terms and provides greater opportunity to achieve principal protection. See " Investment Strategy."

Diverse in-house skills and experience of the Advisor. The Advisor's principals and professionals have diverse and complementary backgrounds, including prior experience at private investment funds, investment banks, other financial services firms, and managing companies. We believe that the diverse professional experience of the Advisor's principals and professionals gives us an advantage in sourcing, evaluating, structuring, negotiating, closing, and profitably exiting investments. The Advisor's advantages include:

- Significant investment expertise in over 30 different industry sectors;
- Track record of leveraged loan originations or participations in original syndications of approximately $5.1 billion to 125 companies since 1999, of which we invested over $1.1 billion in 76 companies;
- Extensive workout and restructuring capabilities honed in multiple in- and out-of-court transactions which allows us to maximize our investment returns and minimize the risk of loss;
- In-house legal expertise with significant experience protecting creditor rights;
- Complementary "bottom-up" and "top-down" (macro economic) expertise; and
- Expertise in analyzing highly complex companies and investments.

Consistent, proactive and rigorous investment and monitoring processes. We believe that the Advisor employs a proven investment process that integrates intensive "bottom-up" company-level research and analysis with a proactive "top-down" view of macroeconomic and industry risks and opportunities. The heart of the process is a thorough analysis of the underlying issuer's business, end markets, competitors, suppliers, revenues, costs, financial statements, and the terms of the issuer's existing obligations, including contingent liabilities (if any). The Advisor's professionals supplement in-house expertise with industry experts, including the Advisor's Board of Advisors and Senior Executive Advisors, as well as other CEO/CFO-level executives, with direct management experience in the industries under consideration. These company level analyses are undertaken in the context of and supplemented by the Advisor's views on and understanding of industry trends and broader economic conditions. These views are formulated and refined through the Advisor's systematic quarterly macroeconomic reviews and quarterly industry reviews, where long-term and immediate macroeconomic trends and their impact on industry risk/reward characteristics are determined. These views flow through to the Advisor's proactive deployment of research and capital resources in the investment process. Quarterly portfolio reviews also help to inform the Advisor's macroeconomic and industry views as well as to inform reporting of deal teams' frequent monitoring of portfolio company progress, risk assessment, and refinement of exit plans.

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Focus on established middle-market companies. We generally invest in companies with established market positions, seasoned management teams, proven and differentiated products and services and strong regional or national operations. We believe that these companies possess better risk-adjusted return profiles than newer companies that are building management or in early stages of building a revenue base. As a specialty middle-market lender, through the Advisor we have proven experience structuring financing for middle-market companies and meeting their specialized needs. We believe that there are fewer experienced finance companies focused on transactions involving small and middle-market companies than larger companies, allowing us to negotiate favorable investment terms, including higher yields, more significant covenant protection, and greater equity grants than typical of transactions involving larger companies. Additionally, we believe that middle-market companies offer significant risk-adjusted return advantages over larger companies as they are generally less able to secure financing compared to larger companies and, we believe, are more likely as borrowers to be subject to upfront fees, prepayment premiums and higher interest rates.

Debt platform with multiple deal sourcing channels. The employees of the Advisor have developed extensive networks among investment bankers, financial advisors, attorneys, private equity sponsors, other senior lenders, high-yield bond specialists, research analysts, accountants, and senior management teams. These networks are a valuable source of directly originated deals and are further supplemented by the networks and experiences of the Advisor's Board of Advisors and Senior Executive Advisors. Additionally, the Advisor's track record as a provider of middle-market financing means that it is often the first or early call on new deal opportunities. Since inception, the Advisor has originated or participated in the original syndication of approximately $5.1 billion of newly issued loans to 125 companies since 1999, of which we invested over $1.1 billion in 76 companies. The Advisor has closed transactions with more than 35 different private equity sponsors. The Advisor is well known as a lender to middle-market companies in a variety of contexts including stressed, distressed, and complex and special situations. The Advisor's in-depth industry knowledge and ability to diligence complex situations thoroughly and in a timely fashion helps to attract deal opportunities from multiple channels.

Attractively priced leverage program. We believe that the Leverage Program (defined below), combined with capital from recent monetizations, provides us with a substantial amount of capital for deployment into new investment opportunities on relatively favorable terms. The Operating Company has an existing $250 million leverage program comprised of: (i) a $116 million senior secured credit facility that matures on July 31, 2016, subject to extension by the lenders at the request of the Operating Company for one 12-month period, which we refer to as the Operating Company Facility; and (ii) $134 million in liquidation preference of preferred interests, which mature on July 31, 2016, which we refer to as the Preferred Interests. The interest rate charged on the Operating Company Facility through July 31, 2014 is LIBOR plus 0.44% per annum. The interest rate charged during the period August 1, 2014 through July 31, 2016, will be LIBOR plus 2.50% per annum. The Operating Company Facility was originally entered into on July 31, 2006 with certain lenders (Variable Funding Capital Company LLC, Versailles CDS LLC and Nieuw Amsterdam Receivables Corp.) and in conjunction with entering into such agreement, the Operating Company also issued the Preferred Interests to such lenders on the same date. TCPC Funding has an existing $100 million revolving credit facility with Deutsch Bank AG, New York Branch, as administrative agent (the "TCPC Funding Facility," and together with the Operating Company Facility, the "Revolving Facilities"). The TCPC Funding Facility contains an accordion feature pursuant to which the credit line may increase up to an aggregate of $200 million, subject to consent of the administrative agent and other customary conditions, and is secured by the assets of TCPC Funding. The TCPC Funding Facility matures on May 15, 2016 and generally bears interest based on LIBOR plus 2.75%, subject to an extension by the lender at TCPC Funding's request for a one year period. The TCPC Funding Facility is secured by all of the assets held by TCPC Funding. We refer to the Revolving Facilities and the Preferred Interests collectively as the Leverage Program. The lenders under the Operating Company Facility also own all of the Operating Company's preferred interests, which is an aggregate of 6,700 Preferred Interests, each of which has a liquidation preference of $20,000 per interest, with dividends generally accruing at an annual rate equal to LIBOR plus 0.85%, subject to certain limitations. For the purpose of the Revolving Facilities, LIBOR means the one-month U.S. dollar deposits which appears on the Telerate Page 3750 as of 11:00 a.m. (London time) on the date the rate is to be determined or as otherwise may be determined pursuant to the Revolving Facilities if such rate does not appear on the Telerate Page 3750. The weighted-average financing rate on the Leverage Program at September 30, 2013 was 1.22%. As preferred shareholders the lenders have the right under the 1940 Act to elect two directors of the Operating Company.

Market opportunity

We believe that the Advisor has a consistent, non-cyclical track record of finding profitable opportunities to lend its managed assets to middle-market companies under most market conditions. However, there can be no assurances that the Advisor will be able to source profitable opportunities of this type for us, and we have a limited record operating as a BDC. We believe that the current environment for direct lending to middle-market companies is especially attractive for several reasons that include:

Reduced lending to middle-market companies by commercial banks. Recent regulatory changes, including the Dodd-Frank Financial Reform Act, or the Dodd-Frank Act, and the introduction of new international capital and liquidity requirements under the Basel III Accords, or Basel III, and the continued ownership of legacy non-performing assets have significantly curtailed banks' lending capacity. In response, we believe that many commercial lenders have de-emphasized their service and product offerings to middle-market companies in favor of lending, managing capital markets transactions and providing other non-credit services to their larger customers. We expect bank lending to middle-market companies to continue to be constrained for several years as Basel III rules phase in and rules and regulations are promulgated and interpreted under the Dodd-Frank Act.

Reduced credit supply to middle-market companies from non-bank lenders. We believe credit to middle-market companies from non-bank lenders will also be constrained as many of those lenders have either gone out of business, exited the market, or are winding down. Numerous hedge funds previously active in leveraged loans disappeared or contracted during the recent financial market crises, while others exited the lending market due to asset-liability mismatches. Other non-bank lenders exited lending due to balance sheet pressures. Furthermore, new collateralized loan obligation, or CLO, formation has been very limited in recent years and existing CLOs' authority to reinvest falls off sharply in coming years. Along with the constraints in bank lending, this situation provides a promising environment in which to originate loans to middle-market companies. We cannot, however, provide any assurance as to the length of time this tight credit supply will persist.

Middle-market companies are increasingly seeking lenders with access to permanent capital for debt and equity capital. We believe that many middle-market companies prefer to borrow from capital providers like us, rather than execute high-yield bond or equity transactions in the public markets that may necessitate increased financial and regulatory compliance and reporting obligations. Further, we believe many middle-market companies are inclined to seek capital from a small number of providers with access to permanent capital that can satisfy their specific needs and can serve as value-added, long-term financial partners with an understanding of the companies' growth needs.

Large Amount of Uninvested Private Equity Capital. Private equity firms raised significant amounts of equity commitments over the period 2006 to 2008, far in excess of the amount of equity they invested. According to Pitchbook, from 2007 to December 2012 there was approximately $328 billion of uninvested capital raised by private equity funds from U.S. investors. We believe the large amount of undeployed private equity capital will drive demand for leveraged buyouts over the next several years, which we believe will, in turn, create significant leveraged lending opportunities for us.

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Significant Refinancing Requirements. A significant portion of the debt associated with a large number of middle-market leveraged mergers and acquisitions completed from 2005 to 2008 matures in the 2013 to 2015 time period. Much of this debt will need to be refinanced as it matures. When combined with the decreased availability of debt financing for middle-market companies generally, we believe these factors should increase lending opportunities for us.

Attractive Pricing and Conservative Deal Structures. We believe that reduced access to, and availability of, debt capital has improved available loan pricing for middle-market lenders. Deals since the recent credit crisis occurred, which began in 2008 and included a period of disruption in the capital markets as evidenced by a lack of liquidity in the debt capital markets, significant write-offs in the financial services sector, the re-pricing of credit risk in the broadly syndicated credit market and the failure of certain major financial institutions, have included meaningful upfront fees, prepayment protections and, in some cases, warrants, all of which should enhance profitability to lenders.

Furthermore, since the credit crisis, lenders generally have required lower leverage levels, increased equity contributions and more comprehensive loan covenants than was customary in the years leading up to the credit crisis. Lower debt multiples on purchase prices suggest that the cash flow of borrowing companies should enable them to service their debt more readily, creating stronger protections against a subsequent downturn.

Company History and BDC Conversion

History

We were organized on July 17, 2006, commenced operations on July 31, 2006 and registered as a non-diversified closed-end management investment company under the 1940 Act. We were formed as a limited liability company under the laws of the State of Delaware, converted to a Delaware corporation on April 2, 2012 and elected BDC status on April 2, 2012.

The Operating Company was formed as a limited partnership under the laws of the State of Delaware. On July 31, 2006, the Operating Company registered as a non-diversified closed-end management investment company under the 1940 Act. The Operating Company issued common limited partner interests to the Holding Company and also issued preferred limited partner interests to the lenders under the Leverage Program. The Operating Company elected to convert from a closed-end fund to a BDC on April 2, 2012. The Holding Company currently conducts its investment operations through the Operating Company. In this regard, the Holding Company will invest substantially all of the net proceeds from the offerings in the common limited partner interests of the Operating Company and the Operating Company, in turn, will invest the proceeds in portfolio companies. See "Use of Proceeds." Following termination of the Revolving Facilities, it is possible that the Operating Company will elect to terminate its existence, in which case it expects to redeem any Preferred Interests then outstanding and transfer its remaining assets to the Holding Company, and the Holding Company expects to continue operations as a stand-alone BDC and make investments directly, rather than through the Operating Company, in accordance with the investment objective and policies described herein. The Operating Company Facility is scheduled to mature on July 31, 2016, subject to a one-year extension at the request of the Operating Company, and the TCPC Funding Facility is scheduled to mature on May 15, 2016, subject to a one-year extension at the request of TCPC Funding. TCPC Funding is a wholly-owned subsidiary of the Operating Company. The Operating Company will transfer certain loans it has originated or acquired or will originate or acquire from time to time to TCPC Funding pursuant to a Sale and Contribution Agreement and various supporting documentation.

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An organizational structure diagram showing our organizational structure is set forth below:

The Holding Company's management consists of the Advisor and its board of directors. The Operating Company's management consists of the Advisor, the General Partner and its board of directors. The board of directors of the Holding Company and the Operating Company are comprised of the same individuals, the majority of whom are independent of the Advisor and the General Partner. The Advisor directs and executes the day-to-day operations of the Holding Company, and the Advisor directs and executes the day-to-day investment operations and the General Partner directs and executes the day-to-day operational activities of the Operating Company, in each case subject to oversight from the respective boards of directors, which set the broad policies of the Holding Company and perform certain functions required by the 1940 Act for the Operating Company. The board of directors of the Operating Company has delegated investment management of the Operating Company's assets to the Advisor, subject to oversight by the board of directors. The managing member of the General Partner is the Advisor, which serves as the investment advisor of each of the Holding Company, the Operating Company and TCPC Funding. Substantially all of the equity interests in the General Partner are owned directly or indirectly by the Advisor, employees of the Advisor and Babson Capital Management, LLC, or Babson. The Holding Company currently owns all of the common interests in the Operating Company and expects to have the ability to maintain that status. While the Operating Company is permitted to issue securities to persons other than the Holding Company, under the Operating Company's limited partnership agreement, board approval is required to issue equity interests of the Operating Company, and the Holding Company directors also serve as the directors of the Operating Company so as to be able to control any issuances by the Operating Company. TCPC Funding is a wholly-owned subsidiary of the Operating Company.

Operating and Regulatory Tax Structure

The Holding Company elected to be treated for U.S. federal income tax purposes as a RIC under the Code. As a RIC, the Holding Company generally does not have to pay corporate-level federal income taxes on any net ordinary income or capital gain that we distribute to our stockholders as dividends if we meet certain source-of-income, distribution and asset diversification requirements. Neither the Operating Company nor TCPC Funding is a RIC, nor will either of them seek RIC status and instead each is intended to be treated as a partnership for tax purposes. The Holding Company and the Operating Company have elected to be treated as BDCs under the 1940 Act. As a BDC we are required to invest at least 70% of our total assets primarily in securities of private and certain U.S. public companies (other than certain financial institutions), cash, cash equivalents, U.S. Government securities, and other high-quality debt investments that mature in one year or less and to comply with other regulatory requirements, including limitations on our use of debt. Because the Holding Company and the Operating Company are each BDCs, their assets, liabilities and results of operations will be consolidated for purposes of this 70% requirement.

Conflicts of Interests

The Advisor and the General Partner currently do, and in the future may, manage funds and accounts other than the Company, which we refer to as the Other Advisor Accounts, with similar investment objectives as the Company. The investment policies, advisor compensation arrangements and other circumstances of the Company may vary from those of Other Advisor Accounts. Accordingly, conflicts may arise regarding the allocation of investments or opportunities among the Company and Other Advisor Accounts. Investments that are suitable for the Company may not be suitable for the Other Advisor Accounts and investments that are suitable for the Other Advisor Accounts may not be suitable for the Company. In certain cases, investment opportunities may be made other than on a pro rata basis. For example, we may desire to retain an asset at the same time that one or more Other Advisor Accounts desire to sell it or we may not have additional capital to invest at a time Other Advisor Accounts do. The Advisor and its affiliates intend to allocate investment opportunities to us and Other Advisor Accounts in a manner that they believe in their judgment and based upon their fiduciary duties to be appropriate considering a variety of factors such as the investment objectives, size of transaction, investable assets, alternative investments potentially available, prior allocations, liquidity, maturity, expected holding period, diversification, lender covenants and other limitations of ours and the Other Advisor Accounts. To the extent that investment opportunities are suitable for the Company and one or more Other Advisor Accounts, the Advisor and the General Partner will allocate investment opportunities pro rata among the Company and Other Advisor Accounts based on the amount of funds each then has available for such investment taking into account these factors. Investment opportunities in certain privately placed securities will be subject to allocation pursuant to the terms of a co-investment exemptive order under the 1940 Act applicable to funds and accounts managed by the Advisor and its affiliates.

There may be situations in which one or more funds or accounts managed by the Advisor or its affiliates might invest in different securities issued by the same company. It is possible that if the company's financial performance and condition deteriorates such that one or both investments are or could be impaired, the Advisor might face a conflict of interest given the difference in seniority of the respective investments. In such situations, the Advisor would review the conflict on a case-by-case basis and implement procedures consistent with its fiduciary duty to enable it to act fairly to each of its clients in the circumstances. Any steps by the Advisor will take into consideration the interests of each of the affected clients, the circumstances giving rise to the conflict, the procedural efficacy of various methods of addressing the conflict and applicable legal requirements.

Company Information

Our administrative and executive offices are located at 2951 28th Street, Suite 1000, Santa Monica, CA 90405, and our telephone number is (310) 566-1094. The Advisor maintains a website at *http://www.tennenbaumcapital.com*. Information contained on this website is not incorporated by reference into this prospectus, and you should not consider information contained on the Advisor's website to be part of this prospectus.

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Risks

Investing in the Company and the shares of common stock offered by this prospectus involves a high degree of risk. These risks, among others, include:

- capital markets experienced a period of disruption and instability, which could return and could have a negative impact on our business and operations and the value of our common stock;
- the risk of credit losses on our investments;
- the risk of loss associated with leverage, illiquidity and valuation uncertainties in our investments, lower amounts of income per share while we are investing the proceeds from the offerings;
- the possible lack of appropriate investments;
- the risk of an inability to renew, extend or replace the Leverage Program, the lack of experience of the Advisor in managing a BDC and our dependence on such investment advisor;
- the risky nature of the securities in which we invest;
- our potential lack of control over our portfolio companies and our limited ability to invest in public or foreign companies;
- the potential incentives to the Advisor to invest more speculatively than it would if it did not have an opportunity to earn incentive compensation;
- our limitations on raising additional capital;
- failure to continue to qualify as a BDC or the risk of loss of tax status as a RIC;
- the risk of volatility in our stock price; and
- the anti-takeover effect of certain provisions in our charter and in the Amended and Restated Limited Partnership Agreement of the Operating Company, or the Amended and Restated Limited Partnership Agreement.

See "Risks" beginning on page 23 of this prospectus for a more detailed discussion of these and other material risks you should carefully consider before deciding to invest in our common stock.

Presentation of Historical Financial Information

Unless otherwise indicated, historical references contained in this prospectus in " Selected Financial Data," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Senior Securities" and "Portfolio Companies" relate to the Holding Company and the Operating Company on a consolidated basis.

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THE OFFERING

We may offer, from time to time, in one or more offerings or series, together or separately, up to $250 million in shares of our common stock, which we expect to use to repay amounts outstanding under the Revolving Facilities, if any, (which will increase the funds under the Revolving Facilities available to us to make additional investments in portfolio companies) and to use the remainder to make investments in portfolio companies in accordance with our investment objective and for other general corporate purposes, including payment of operating expenses.

Shares of our common stock may be offered directly to one or more purchasers, through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to a particular offering will disclose the terms of that offering, including the name or names of any agents, underwriters or dealers involved in the sale of shares of our common stock, the purchase price, and any fee, commission or discount arrangement between us and our agents, underwriters or dealers, or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell shares of our common stock through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of such shares of our common stock.

Set forth below is additional information regarding the offering of shares of our common stock:

The Nasdaq Global Select Market Symbol	"TCPC"
Use of Proceeds	Unless otherwise specified in a prospectus supplement, we intend to use the net proceeds to reduce our borrowings outstanding under the Revolving Facilities, if any, and to make investments in portfolio companies in accordance with our investment objective and for other general corporate purposes, including payment of operating expenses. Pending investment, we may invest the remaining net proceeds of the offerings primarily in cash, cash equivalents, U.S. Government securities and other high-quality debt investments that mature in one year or less. These securities may have lower yields than our other investments and accordingly may result in lower distributions, if any, during such period. See "Use of Proceeds."
Investment Management Arrangements	The Holding Company and the Operating Company have entered into separate but substantially identical investment management agreements with the Advisor, under which the Advisor, subject to the overall supervision of our respective boards of directors, manages the day-to-day operations of and provides investment advisory services to the Holding Company and the Operating Company. For providing these services, the Advisor receives a base management fee calculated at an annual rate of 1.5% of our total assets (excluding cash and cash equivalents) on a consolidated basis, payable quarterly in arrears. For purposes of calculating the base management fee, "total assets" is determined without deduction for any borrowings or liabilities.

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The investment management agreements also provide for performance based returns to the Advisor or the General Partner (referred to herein as "incentive compensation"). Under the investment management agreements and the Amended and Restated Limited Partnership Agreement, no incentive compensation was incurred until after January 1, 2013.

The incentive compensation is calculated as the sum of (1) 20% of all ordinary income since January 1, 2013 and (2) 20% of all net realized capital gains (net of any net unrealized capital depreciation) since January 1, 2013, with each component being subject to a total return limitation of 8% of contributed common equity. The incentive compensation initially is payable by making an equity allocation to the General Partner under the Operating Company's Amended and Restated Limited Partnership Agreement. If the Operating Company is terminated or for any other reason incentive compensation is not distributed by the Operating Company, it would be paid pursuant to the investment management agreement between the Holding Company and the Advisor.

The incentive compensation has two components, ordinary income and capital gains. Each of the two components of incentive compensation is separately subject to a total return limitation. Thus, we are not obligated to pay or distribute any ordinary income incentive compensation or any capital gains incentive compensation if the cumulative total return does not exceed an 8% annual return on daily weighted average contributed common equity. If such cumulative total return does exceed 8%, we are not obligated to pay or distribute any ordinary income incentive compensation or any capital gains incentive compensation to the extent such amount would exceed 20% of the cumulative total return of the Company that exceeds a 10% annual return on daily weighted average contributed common equity, plus all of the cumulative total return that exceeds an 8% annual return on daily weighted average contributed common equity but is not more than a 10% annual return on daily weighted average contributed common equity, less cumulative incentive compensation previously paid or distributed (whether on ordinary income or capital gains).

Subject to the above limitation, the ordinary income component of incentive compensation is the amount, if positive, equal to 20% of the cumulative ordinary income before incentive compensation, less cumulative ordinary income incentive compensation previously paid or distributed.

Subject to the above limitation, the capital gains component of the incentive compensation is the amount, if positive, equal to 20% of the cumulative realized capital gains (computed net of cumulative realized losses and cumulative unrealized capital depreciation), less cumulative capital gains incentive compensation previously paid or distributed.

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	For purposes of the foregoing computations and the total return limitation, the relevant terms are defined in detail in the section entitled "Management of the Company Investment Management Agreements." The base management fee is paid by the Operating Company to the Advisor and the incentive compensation, if any, is distributed by the Operating Company to the General Partner. The Holding Company, therefore, indirectly bears these amounts, which are reflected in our consolidated financial statements. If the Operating Company is terminated or for any other reason incentive compensation is not paid by the Operating Company, such compensation would be paid to the Advisor directly by the Holding Company pursuant to its investment management agreement with the Advisor to ensure that the appropriate aggregate amount of incentive compensation is paid. On a consolidated basis, the aggregate compensation is limited to 1.5% of total assets and 20% of the relevant components of income and realized capital gains. See "Management of the Company Investment Management Agreements" for a more detailed description of the investment management arrangements.
Distributions	We intend to make quarterly distributions to our stockholders. The timing and amount of our quarterly distributions, if any, is determined by our board of directors. Any distributions to our stockholders are declared out of assets legally available for distribution. In addition, because we will invest substantially all of our assets in the Operating Company, we are only able to pay distributions on our common stock from distributions received from the Operating Company. The Operating Company intends to make distributions that are sufficient to enable us to pay quarterly distributions to our stockholders and maintain our status as a regulated investment company, or a RIC. While it is intended that the distributions made by the Operating Company are sufficient to enable us to pay quarterly distributions to our stockholders and maintain our status as a RIC, there can be no assurances that the distributions from the Operating Company are sufficient to pay distributions to our stockholders in the future.
Taxation	The Holding Company currently is a RIC for U.S. federal income tax purposes and intends to continue to qualify each year as a RIC. In order to qualify as a RIC, the Holding Company generally must satisfy certain income, asset diversification and distribution requirements. As long as it so qualifies, the Holding Company will not be subject to U.S. federal income tax to the extent that it distributes its investment company taxable income and net capital gain on a timely basis. The Holding Company will invest substantially all of the net proceeds from the offerings in the Operating Company, which is treated as a partnership for U.S. federal income tax purposes. Consequently, any references to, and description of, the U.S. federal income tax aspects of the Holding Company's investment practices and activities, in effect, takes into account the investment practices and activities of the Operating Company. See "Distributions" and "U.S. Federal Income Tax Matters."

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Custodian	Wells Fargo Bank, National Association, or the Custodian, serves as our custodian. See "Custodian."
Transfer and Dividend Paying Agent	Wells Fargo Bank, National Association, or Wells Fargo, serves as our Transfer and Dividend Paying Agent. See "Transfer Agent."
Borrowings and Preferred Stock	We expect to use leverage, including through the Revolving Facilities, to make investments. We are exposed to the risks of leverage, which include that leverage may be considered a speculative investment technique. The use of leverage magnifies the potential for gain and loss on amounts invested by us and therefore increases the risks associated with investing in shares of our common stock. The Holding Company and the Operating Company will, on a consolidated basis, comply with the asset coverage and other requirements relating to the issuance of senior securities under the 1940 Act. Because the base investment advisory fee we pay the Advisor is calculated by reference to our total assets, the Advisor may have an incentive to increase our leverage in order to increase its fees. See "Risks."
Trading at a Discount	Shares of closed-end investment companies, including business development companies, frequently trade at a discount from their net asset value. We are not generally able to issue and sell our common stock at a price below our net asset value per share unless we have stockholder approval. At our 2013 annual meeting, held on May 1, 2013, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering, our stockholders approved our ability to sell or otherwise issue shares of our common stock at any level of discount from net asset value per share for a twelve month period expiring on the anniversary of the date of stockholder approval. The possibility that our shares may trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline. Our net asset value immediately following an offering will reflect reductions resulting from the sales load and the amount of such offering expenses paid by us. This risk may have a greater effect on investors expecting to sell their shares soon after completion of such offering, and our shares may be more appropriate for long-term investors than for investors with shorter investment horizons. We cannot predict whether our shares will trade above, at or below net asset value. See "Risks."

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Dividend Reinvestment Plan	We have a dividend reinvestment plan for our stockholders. This is an "opt in" dividend reinvestment plan. As a result, if we declare a cash dividend or other distribution payable in cash, each stockholder that has not "opted in" to our dividend reinvestment plan will receive such dividends in cash, rather than having their dividends automatically reinvested in additional shares of our common stock. Stockholders who receive distributions in the form of shares of common stock will be subject to the same U.S. federal, state and local tax consequences as if they received their distributions in cash. See "Dividend Reinvestment Plan."
Anti-Takeover Provisions	Our certificate of incorporation and the Amended and Restated Limited Partnership Agreement as well as certain statutory and regulatory requirements, contain certain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. These anti-takeover provisions may inhibit a change in control in circumstances that could give the holders of our common stock the opportunity to realize a premium over the market price for our common stock. See "Description of Securities."
Administrator	Under a separate administration agreement, the General Partner serves as our Administrator. As Administrator, the General Partner oversees our financial records, prepares reports to our stockholders and reports filed with the SEC, leases office space to us, provides us with equipment and office services and generally monitors the payment of our expenses and provides or supervises the performance of administrative and professional services used by us. We reimburse the Administrator for its costs in providing these services without paying any separate administration fee, markup or other profit in excess of fully allocated costs. Although the Administrator has waived these reimbursements through December 31, 2012, it discontinued such waiver starting at January 1, 2013. There is no predetermined limit on such expenses, however, reimbursement for any such expenses are subject to the review and approval of our board of directors.
License Agreement	We have entered into a royalty-free license agreement with the Advisor, pursuant to which the Advisor has agreed to grant us a non-exclusive license to use the name "TCP."
Available Information	We have filed with the SEC a registration statement on Form N-2 under the Securities Act of 1933, as amended, or the Securities Act, which contains additional information about us and the shares of our common stock being offered by this prospectus. We are obligated to file annual, quarterly and current reports, proxy statements and other information with the SEC. This information is available at the SEC's public reference room in Washington, D.C. and on the SEC's website at *http://www.sec.gov*. See "Additional Information."

The Advisor maintains a website at *http://www.tennenbaumcapital.com* and we make all of our annual, quarterly and current reports, proxy statements and other publicly filed information, including the SAI, which is incorporated by reference in this prospectus, available, free of charge, on or through this website. You may also obtain such information by contacting us at 2951 28th Street, Suite 1000, Santa Monica, CA 90405, or by calling us collect at (310) 566-1094. Information contained on the Advisor's website is not incorporated by reference into this prospectus, and you should not consider information contained on the Advisor's website to be part of this prospectus.

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FEES AND EXPENSES

The following table is intended to assist you in understanding the costs and expenses that an investor in our common stock will bear directly or indirectly. **The following table and example should not be considered a representation of our future expenses. Actual expenses may be greater or less than shown**. The following table and example represent our best estimate of the fees and expenses that we expect to incur during the next twelve months. Further, the fees and expenses below are presented on a consolidated basis directly or indirectly to include expenses of the Company and the Operating Company that investors in our common stock offering will bear.

Stockholder Transaction Expenses	
Sales Load (as a percentage of offering price)	%(1)
Offering Expenses (as a percentage of offering price)	%(2)
Dividend Reinvestment Plan Fees	(3)
Total Stockholder Transaction Expenses (as a percentage of offering price)	%
Annual Expenses (as a Percentage of Net Assets Attributable to Common Stock)(4)	
Base Management Fees	2.56%(5)
Incentive Compensation Payable Under the Investment Management Agreement (20% of ordinary income and capital gains)	2.38%(6)
Interest Payments on Borrowed Funds	0.86%(7)
Preferred Dividends	0.26%(8)
Other Expenses	0.58%(9)
Total Annual Expenses	6.64%

(1) In the event that the shares of common stock to which this prospectus relates are sold to or through underwriters, a corresponding prospectus supplement will disclose the estimated applicable sales load.

(2) The related prospectus supplement will disclose the estimated amount of offering expenses, the offering price and the estimated offering expenses borne by us as a percentage of the offering price.

(3) The expenses of the dividend reinvestment plan are included in "other expenses." See "Dividend Reinvestment Plan."

(4) The "net assets attributable to common stock" used to calculate the percentages in this table is our average assets of $352.5 million for the 12 month period ended September 30, 2013. The related prospectus supplement will disclose the offering price and the total stockholder transaction expenses as a percentage of the offering price.

(5) Base management fees are paid quarterly in arrears. The base management fee of 1.5% is calculated based on the value of our total assets (excluding cash and cash equivalents) at the end of the most recently completed calendar quarter. The percentage shown in the table, which assumes all capital and leverage is invested at the maximum level, is calculated by determining the ratio that the aggregate base management fee bears to our net assets attributable to common stock and not total assets. We make this conversion because all of our interest and preferred stock dividend payments are indirectly borne by our common stockholders. If we borrow money or issue preferred stock and invest the proceeds other than in cash and cash equivalents, our base management fees will increase. The base management fee for any partial quarter is appropriately pro rated. See "Management of the Company   Investment Management Agreements."

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(6) Under the investment management agreements and the Amended and Restated Limited Partnership Agreement, no incentive compensation was incurred until after January 1, 2013. The incentive compensation has two components, ordinary income and capital gains. Each component is payable quarterly in arrears (or upon termination of the Advisor as the investment manager or the General Partner as of the termination date) and is calculated based on the cumulative return for periods beginning January 1, 2013 and ending on the relevant calculation date.

Each of the two components of incentive compensation is separately subject to a total return limitation. Thus, notwithstanding the following provisions, we are not obligated to pay or distribute any ordinary income incentive compensation or any capital gains incentive compensation if our cumulative total return does not exceed an 8% annual return on daily weighted average contributed common equity. The incentive compensation we would pay is subject to a total return limitation. That is, no incentive compensation is paid if our cumulative annual total return is less than 8% of our average contributed common equity. If our cumulative annual total return is above 8%, the total cumulative incentive compensation we pay is not more than 20% of our cumulative total return, or, if lower, the amount of our cumulative total return that exceeds the 8% annual rate.

Subject to the above limitation, the ordinary income component is the amount, if positive, equal to 20% of the cumulative ordinary income before incentive compensation, less cumulative ordinary income incentive compensation previously paid or distributed.

Subject to the above limitation, the capital gains component is the amount, if positive, equal to 20% of the cumulative realized capital gains (computed net of cumulative realized losses and cumulative net unrealized capital depreciation), less cumulative capital gains incentive compensation previously paid or distributed. For assets held on January 1, 2013, capital gain, loss and depreciation are measured on an asset by asset basis against the value thereof as of December 31, 2012. The capital gains component will be paid or distributed in full prior to payment or distribution of the ordinary income component.

(7) "Interest Payments on Borrowed Funds" represents dividends, interest and fees estimated to be accrued on the Revolving Facilities and amortization of debt issuance costs, and assumes the Revolving Facilities is fully drawn (subject to asset coverage limitations under the 1940 Act) and that the interest rate on the debt issued (i) under the Operating Company Facility is the rate in effect as of September 30, 2013, which was 0.62% and (ii) under the TCPC Funding Facility is the rate in effect as of September 30, 2013, which was 3.02%. When we borrow money or issue preferred stock, all of our interest and preferred stock dividend payments are indirectly borne by our common stockholders.

(8) "Preferred Dividends" represents dividends estimated to be accumulated on the Preferred Interests and assumes that the dividend rate on the Preferred Interests is the rate in effect as of September 30, 2013, which was 1.03%. When we borrow money or issue preferred stock, all of our interest and preferred stock dividend payments are indirectly borne by our common stockholders.

(9) "Other Expenses" includes our estimated overhead expenses, including expenses of the Advisor reimbursable under the investment management agreements and of the Administrator reimbursable under the administration agreement except for certain administration overhead costs which are not currently contemplated to be charged to us. Such expense estimate, other than the Administrator expenses, is based on actual other expenses for the three months ended September 30, 2013.

Example

The following example demonstrates the projected dollar amount of total cumulative expenses (including stockholder transaction expenses and annual expenses) that would be incurred over various

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periods with respect to a hypothetical investment in our common stock. In calculating the following expense amounts, we have assumed that our annual operating expenses remain at the levels set forth in the table above.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return	$ 72	$ 156	$ 241	$ 459

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. There is no incentive compensation either on income or on capital gains under our investment management agreements and the Amended and Restated Limited Partnership Agreement assuming a 5% annual return and therefore it is not included in the example. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive compensation of a material amount, our distributions to our common stockholders and our expenses would likely be higher. In addition, while the example assumes reinvestment of all dividends and distributions at net asset value, participants in our dividend reinvestment plan will receive a number of shares of our common stock, determined by dividing the total dollar amount of the dividend or distribution payable to a participant by the market price per share of our common stock at the close of trading on the valuation date for the dividend. See "Dividend Reinvestment Plan" for additional information regarding our dividend reinvestment plan.

Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by "you," the "Company," the "Holding Company," the "Operating Company" or "us," our common stockholders will indirectly bear such fees or expenses, including through the Company's investment in the Operating Company.

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SELECTED FINANCIAL DATA

The selected consolidated financial and other data below reflects the consolidated historical operations of the Holding Company and the Operating Company. This consolidated financial and other data is the Holding Company's historical financial and other data. The Operating Company will continue to be the Holding Company's sole investment following the completion of this offering.

The selected consolidated financial data below for the years ended December 31, 2012, 2011, 2010, 2009 and 2008 has been derived from the consolidated financial statements that were audited by our independent registered public accounting firm. This selected financial data should be read in conjunction with our financial statements and related notes thereto, which are incorporated by reference into this prospectus and the SAI, and "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Senior Securities" included elsewhere in this prospectus.

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The historical and future financial information may not be representative of the Company's financial information in future periods.

	For the Year Ended December 31,				
	2012	2011	2010	2009	2008
Performance Data:					
Interest income	$ 49,243,332	$ 42,113,358	$ 32,410,819	$ 26,678,140	$ 34,719,010
Dividend income	1,811,189	10,610,159	13,547,924		2,250,032
Other income	1,138,238	2,134,159	1,842,469	417,533	238,994
Total investment income	52,192,759	54,857,676	47,801,212	27,095,673	37,208,036
Interest and credit agreement expenses	857,757	942,288	893,806	949,554	5,314,342
Investment advisory expense	6,908,942	6,787,188	6,787,188	6,787,188	8,287,188
Other expenses	4,105,700	1,520,474	1,213,685	1,426,099	1,086,533
Total expenses	11,872,399	9,249,950	8,894,679	9,162,841	14,688,063
Net investment income	40,320,360	45,607,726	38,906,533	17,932,832	22,519,973
Realized and unrealized gains (losses)	(12,784,251)	(38,878,881)	31,621,019	36,142,346	(209,274,336)
Dividends to preferred interest holders	(1,602,799)	(1,545,555)	(1,519,759)	(1,740,964)	(5,190,988)
Minority interest					3,149,915
Net increase (decrease) in net assets from operations	$ 25,933,310	$ 5,183,290	$ 69,007,793	$ 52,334,214	$ (188,795,436)
Per Share Data (at the end of the period):*					
Net increase (decrease) in net assets from operations	$ 1.21	$ 12.37	$ 164.72	$ 124.92	$ (450.63)
Distributions declared per share	(1.43)	(75.19)	(89.99)	(36.28)	(19.10)
Average weighted shares outstanding for the period	21,475,847	418,956	418,956	418,956	418,956

* Per share amounts prior to the Conversion on April 2, 2012 are calculated based on 418,956 shares outstanding. Per share amounts subsequent to the Conversion are calculated on 21,475,847 weighted-average shares outstanding.

	For the Year Ended December 31,				
	2012	2011	2010	2009	2008
Assets and Liabilities Data:					
Investments	517,683,087	378,960,536	453,034,872	343,062,967	348,504,225
Other assets	31,559,015	24,492,967	20,604,286	119,642,507	19,677,567
Total assets	549,242,102	403,453,503	473,639,158	462,705,474	368,181,792
Amount drawn on credit facility	74,000,000	29,000,000	50,000,000	75,000,000	34,000,000
Other liabilities	24,728,267	2,116,211	25,050,178	20,431,955	3,239,231
Total liabilities	98,728,267	31,116,211	75,050,178	95,431,955	37,239,231
Preferred stock			23,527	25,391	23,516
Preferred limited partner interests	134,526,285	134,466,418	134,377,869	134,368,337	135,173,468
Minority interest					
Net assets	$ 315,987,550	$ 237,870,874	$ 264,187,584	$ 232,879,791	$ 195,745,577
Investment Activity Data:					
No. of portfolio companies at period end	54	41	44	40	27

Acquisitions	$ 359,020,926	$ 171,842,663	$ 262,837,727	$ 144,313,178	$ 169,262,403
Sales, repayments, and other disposals	$ 211,216,033	$ 216,916,444	$ 192,419,667	$ 195,383,341	$ 257,415,641
Weighted-Average Yield on debt investments at end of period	11.3%	14.1%	13.1%	12.5%	18.5%

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RISKS

Before you invest in our common stock, you should be aware of various risks, including those described below. You should carefully consider these risk factors, together with all of the other information included in this prospectus, including our consolidated financial statements and the related notes thereto, before you decide whether to make an investment in our common stock. The risks set out below are not the only risks we face, but they are the principal risks associated with an investment in the Company or generally associated with investment in a company with investment objectives, investment policies, capital structure or trading markets similar to the Company's. Additional risks and uncertainties not currently known to us or that are currently immaterial also may materially adversely affect our business, financial condition and/or operating results. If any of the following events occur, our business, financial condition and results of operations could be materially adversely affected. In such case, our net asset value and the trading price of our common stock could decline, and you may lose all or part of your investment.

Certain risks in the current environment

Capital markets have experienced a period of disruption and instability. These market conditions have materially and adversely affected debt and equity capital markets in the United States and abroad, which could have a negative impact on our business and operations.

The global capital markets have experienced a period of disruption as evidenced by a lack of liquidity in the debt capital markets, significant write-offs in the financial services sector, the re-pricing of credit risk in the broadly syndicated credit market and the failure of certain major financial institutions. Despite actions of the United States federal government and foreign governments, these events contributed to worsening general economic conditions that materially and adversely impacted the broader financial and credit markets and reduced the availability of debt and equity capital for the market as a whole and financial services firms in particular. These conditions have ameliorated significantly, but could return or worsen in the future. While these conditions persist, we and other companies in the financial services sector may be required to, or may choose to, seek access to alternative markets for debt and equity capital. Equity capital may be difficult to raise because, subject to some limited exceptions, as a BDC we are not generally able to issue and sell our common stock at a price below net asset value per share without first obtaining approval for such issuance from our stockholders and independent directors. At our annual meeting of stockholders held on December 7, 2012, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering, our stockholders approved our ability to sell or otherwise issue shares of our common stock at a price below its then current net asset value per share for a twelve month period expiring on the anniversary of the date of stockholder approval. It should be noted that, theoretically, we may offer up to 25% of our then outstanding common stock each day. In addition, the debt capital that will be available, if at all, may be at a higher cost, and on less favorable terms and conditions in the future. In addition, the portfolio companies in which we invest may not be able to service or refinance their debt, which could materially and adversely affect our financial condition as we could experience reduced income or even losses. The inability to raise capital and the risk of portfolio company defaults may have a negative effect on our business, financial condition and results of operations.

Moreover, recent market conditions have made, and may in the future make, it difficult to extend the maturity of or refinance our existing indebtedness and any failure to do so could have a material adverse effect on our business. The illiquidity of our investments may make it difficult for us to sell such investments if required. As a result, we may realize significantly less than the value at which we have recorded our investments.

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The current financial market situation, as well as various social and political tensions in the United States and around the world, particularly in the Middle East, may continue to contribute to increased market volatility, may have long-term effects on the United States and worldwide financial markets, and may cause further economic uncertainties or deterioration in the United States and worldwide. Since 2010, several European Union ("EU") countries, including Greece, Ireland, Italy, Spain, and Portugal, have faced budget issues, some of which may have negative long-term effects for the economies of those countries and other EU countries. There is continued concern about national-level support for the euro and the accompanying coordination of fiscal and wage policy among European Economic and Monetary Union member countries. The Advisor does not know how long the financial markets will continue to be affected by these events and cannot predict the effects of these or similar events in the future on the United States economy and securities markets or on our investments. The Advisor monitors developments and seeks to manage our investments in a manner consistent with achieving our investment objective, but there can be no assurance that it will be successful in doing so; and the Advisor may not timely anticipate or manage existing, new or additional risks, contingencies or developments, including regulatory developments in the current or future market environment.

Capital markets volatility also affects our investment valuations. While most of our investments are not publicly traded, applicable accounting standards require us to assume as part of our valuation process that our investments are sold in a principal market to market participants (even if we plan on holding an investment through its maturity). As a result, volatility in the capital markets can adversely affect our valuations.

Risks related to our business

We may not replicate the Company's historical performance or the historical performance of other entities managed or supported by the Advisor.

We may not be able to replicate the Company's historical performance or the historical performance of the Advisor's investments, and our investment returns may be substantially lower than the returns achieved by the Company in the past. We can offer no assurance that the Advisor will be able to continue to implement our investment objective with the same degree of success as it has had in the past.

We may suffer credit losses.

Investment in middle-market companies is highly speculative and involves a high degree of risk of credit loss, and therefore our securities may not be suitable for someone with a low tolerance for risk. These risks are likely to increase during an economic recession, such as the United States and many other economies recently experienced or are currently experiencing.

Our use of borrowed funds and preferred securities, including under the Leverage Program, to make investments exposes us to risks typically associated with leverage.

The Operating Company borrows money, directly and indirectly through TCPC Funding, and has the Preferred Interests outstanding through the Leverage Program. As a result:

- our common stock is exposed to incremental risk of loss and a decrease in the value of our investments would have a greater negative impact on the value of our common stock than if we did not use leverage;

- adverse changes in interest rates could reduce or eliminate the incremental income we make with the proceeds of any leverage;

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- we, and indirectly our common stockholders, bear the entire cost of issuing and paying interest or dividends on any borrowed funds or preferred securities issued by us or the Operating Company;

- our ability to pay dividends on our common stock will be restricted if our asset coverage ratio is not at least 200% and any amounts used to service indebtedness or preferred stock would not be available for such dividends; and

- our ability to amend the Operating Company organizational documents or investment management agreements may be restricted if such amendment could have a material adverse impact on the lenders under our Leverage Program.

The Preferred Interests have similar risks to our common stockholders as borrowings. Such preferred securities rank "senior" to common stock in our capital structure, resulting in such preferred securities having certain separate voting rights, dividend and liquidation rights, and possibly other rights, preferences or privileges more favorable than those granted to holders of our common stock. For example, payment of dividends and repayment of the liquidation preference of the Preferred Interests takes preference over any dividends or other payments to our common stockholders, and preferred holders are not subject to any of our expenses or losses. Furthermore, our Preferred Interests and the issuance of any additional preferred securities could delay, defer or prevent a transaction or a change of control that might involve a premium price for our common stockholders or otherwise be in your best interest.

The use of leverage creates increased risk of loss and is considered a speculative investment technique. The use of leverage magnifies the potential gains and losses from an investment and increases the risk of loss of capital. To the extent that income derived by us from investments purchased with borrowed funds or the issuances of preferred stock is greater than the cost of borrowing or issuing and servicing the preferred stock, our net income will be greater than if borrowing had not been used. Conversely, if the income from investments purchased from these sources is not sufficient to cover the cost of the leverage, our net investment income will be less than if leverage had not been used, and the amount available for ultimate distribution to the holders of common stock will be reduced. The extent to which the gains and losses associated with leveraged investing are increased will generally depend on the degree of leverage employed. We may, under some circumstances, be required to dispose of investments under unfavorable market conditions in order to maintain our leverage, thus causing us to recognize a loss that might not otherwise have occurred. In the event of a sale of investments upon default under our borrowing arrangements, secured creditors will be contractually entitled to direct such sales and may be expected to do so in their interest, rather than in the interests of the holders of common stock. Holders of common stock will incur losses if the proceeds from a sale in any of the foregoing circumstances are insufficient, after payment in full of amounts due and payable on leverage, including administrative expenses, to repay such holders investments in our common stock. As a result, you could experience a total loss of your investment. Any decrease in our revenue would cause our net income to decline more than it would have had we not borrowed funds and could negatively affect our ability to make distributions on our common stock. The ability to service any debt or the Preferred Interests that we have or may have outstanding depends largely on our financial performance and is subject to prevailing economic conditions and competitive pressures. There is no limitation on the percentage of portfolio investments that can be pledged to secure borrowings. The amount of leverage that we employ at any particular time will depend on the Advisor's and our board of director's assessments of market and other factors at the time of any proposed borrowing.

In addition to regulatory restrictions that restrict our ability to raise capital, the Leverage Program contains various covenants which, if not complied with, could accelerate repayment under the Revolving Facilities or require redemption of the Preferred Interests, thereby materially and adversely affecting our liquidity, financial condition and results of operations.

Under the Leverage Program, we must comply with certain financial and operational covenants. These covenants include:

- restrictions on the level of indebtedness that we are permitted to incur and the number of Preferred Interests we are permitted to have outstanding in relation to the value of our assets;
- restrictions on our ability to make distributions and other restricted payments under certain circumstances;
- restrictions on extraordinary events, such as mergers, consolidation and sales of assets;
- restrictions on our ability to incur liens and incur indebtedness; and
- maintenance of a minimum level of stockholders' equity.

In addition, by limiting the circumstances in which borrowings may occur under the Revolving Facilities, the credit agreements related to the Revolving Facilities, or the Credit Agreements, in effect provides for various asset coverage, credit quality and diversification limitations on our investments. Such limitations may cause us to be unable to make or retain certain potentially attractive investments or to be forced to sell investments at an inappropriate time and consequently impair our profitability or increase losses or result in adverse tax consequences. As of December 3, 2013, we were in compliance with these covenants. However our continued compliance with these covenants depends on many factors, some of which are beyond our control. Accordingly, there are no assurances that we will continue to comply with the covenants in the Credit Agreements. Failure to comply with these covenants would result in a default under the Credit Agreements which, if we were unable to obtain a waiver from the lenders thereunder, could result in an acceleration of repayments under the Credit Agreements. In addition, a default under the Credit Agreements will, in certain circumstances, require the Preferred Interests to be redeemed. As such, failure to comply with these covenants could have a material adverse impact on our business, financial condition and results of operations.

The Operating Company Facility also has certain "key man" provisions. For example, it is an event of default if any of Michael E. Tennenbaum, Howard M. Levkowitz or Mark K. Holdsworth ceases to be actively involved in the management of the Advisor and is not replaced with someone with comparable skills within 180 days. Further, if any two of the individuals cease to be actively involved in management of the Advisor, the administrative agent under the Operating Company's Credit Agreement may veto a proposed replacement for one of such individuals and may veto any of the Operating Company's portfolio transactions that are in excess of 15% of its total assets until a replacement has been appointed to fill one of such positions.

The Operating Company Facility matures in July 2016, the TCPC Funding Facility matures in May 2016 and the Preferred Interests will be subject to mandatory redemption in July 2016. Any inability to renew, extend or replace the Revolving Facilities or replace the Preferred Interests could adversely impact our liquidity and ability to find new investments or maintain distributions to our stockholders.

The Operating Company Facility matures July 31, 2016, subject to extension by the lenders at our request for one 12-month period. Advances under the Operating Company Facility generally bear interest at LIBOR plus 0.44% through July 31, 2014 and LIBOR plus 2.50% during the period August 1, 2014 through July 31, 2016, in each case subject to certain limitations. The TCPC Funding Facility matures on May 15, 2016, subject to an extension by the lender at TCPC Funding's request for a 12-month period. Advances under the TCPC Funding Facility generally bears interest based on

LIBOR plus 2.75%, subject to certain limitations. The Preferred Interests will be subject to mandatory redemption on July 31, 2016. We do not currently know whether we will renew, extend or replace the Revolving Facilities upon their maturities or replace the Preferred Interests, or if we do either or both, whether we will be able to do so on terms that are as favorable as the Revolving Facilities or Preferred Interests, respectively. In addition, we will be required to liquidate assets to repay amounts due under the Revolving Facilities or the Preferred Interests if we do not renew, extend or replace the Revolving Facilities or Preferred Interests prior to their respective maturities.

Upon the termination of the Revolving Facilities, there can be no assurance that we will be able to enter into a replacement facility on terms that are as favorable to us, if at all. We expect that any facility we enter into will likely be on terms less favorable than currently contained in the Operating Company Facility. Our ability to replace the Revolving Facilities may be constrained by then-current economic conditions affecting the credit markets. In the event that we are not able to replace the Revolving Facilities at the time of their maturity, this could have a material adverse effect on our liquidity and ability to fund new investments, our ability to make distributions to our stockholders and our ability to qualify as a RIC.

The creditors under the Revolving Facilities have a first claim on all of the Company's assets included in the collateral for the Revolving Facilities.

Lenders have fixed dollar claims on our assets that are superior to the claims of our common stockholders or any preferred holders. Substantially all of our current assets have been pledged as collateral under the Revolving Facilities. If an event of default occurs under the Revolving Facilities, the lenders would be permitted to accelerate amounts due under the Revolving Facilities and liquidate our assets to pay off amounts owed under the Revolving Facilities and limitations would be imposed on us with respect to the purchase or sale of investments. Such limitations may cause us to be unable to make or retain certain potentially attractive investments or to be forced to sell investments at an inappropriate time and consequently impair our profitability or increase our losses or result in adverse tax consequences.

In the event of the dissolution of the Operating Company or otherwise, if the proceeds of the Operating Company's assets (after payment in full of obligations to any such debtors and of any liquidation preference to any holders of preferred stock) are insufficient to repay capital invested in us by the holders of the common stock, no other assets will be available for the payment of any deficiency. None of our board of directors, the Advisor, the General Partner or any of their respective affiliates, have any liability for the repayment of capital contributions made to the Company by the holders of common stock. Holders of common stock could experience a total loss of their investment in the Company.

Lenders under the Operating Company Facility may have a veto power over the Company's investment policies.

If a default has occurred under the Operating Company Facility, the lenders under the Operating Company Facility may veto changes in investment policies. The Operating Company Facility also has certain limitations on unusual types of investments such as commodities, real estate and speculative derivatives, which are not part of the Company's investment strategy or policies in any event.

The lack of liquidity in substantially all of our investments may adversely affect our business.

Our investments generally are made and will continue to be made in private companies. Substantially all of these securities will be subject to legal and other restrictions on resale or will be otherwise less liquid than publicly traded securities. The illiquidity of our investments may make it difficult for us to sell such investments if the need arises. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we had previously recorded our investments. Further, we may face other restrictions on our ability to liquidate an investment in a portfolio company to the extent that we or an affiliated manager has material non-public information regarding such portfolio company.

A substantial portion of our portfolio investments may be recorded at fair value as determined in good faith by or under the direction of our board of directors and, as a result, there may be uncertainty regarding the value of our portfolio investments.

The debt and equity investments that we make for which market quotations are not readily available will be valued at fair value as determined in good faith by or under the direction of our board of directors. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material. Our net asset value could be adversely affected if determinations regarding the fair value of these investments were materially higher than the values ultimately realized upon the disposal of such investments.

We are exposed to risks associated with changes in interest rates.

General interest rate fluctuations may have a substantial negative impact on our investments, the value of our common stock and our rate of return on invested capital. A reduction in the interest rates on new investments relative to interest rates on current investments could also have an adverse impact on our net investment income. An increase in interest rates could decrease the value of any investments we hold that earn fixed interest rates, including subordinated loans, senior and junior secured and unsecured debt securities and loans and high-yield bonds, and also could increase our interest expense, thereby decreasing our net income. Also, an increase in interest rates available to investors could make investment in our common stock less attractive if we are not able to increase our dividend rate, which could reduce the value of our common stock.

The Advisor may face conflicts in allocating investment opportunities between us and certain other entities that could adversely impact our investment returns.

The Advisor and its affiliates, employees and associates currently do and in the future may manage other funds and accounts, including for other accounts in which certain holders of our common stock have investments, which we refer to as Other Advisor Accounts. Other Advisor Accounts invest in assets that are also eligible for purchase by us. Our investment policies, fee arrangements and other circumstances may vary from those of Other Advisor Accounts. Accordingly, conflicts may arise regarding the allocation of investments or opportunities among us and Other Advisor Accounts. In general, the Advisor and its affiliates will allocate investment opportunities pro rata among us and Other Advisor Accounts (assuming the investment satisfies the objectives of each) based on the amount of committed capital each then has available. The allocation of certain investment opportunities in private placements is subject to independent director approval pursuant to the terms of the co-investment exemptive order applicable to us and described below. In certain cases, investment opportunities may be made other than on a pro rata basis. For example, we may desire to retain an asset at the same time that one or more Other Advisor Accounts desire to sell it or we may not have additional capital to invest at a time Other Advisor Accounts do. When our investment allocations are made on a basis other than pro rata our investment performance may be less favorable when compared to the investment performance of Other Advisor Accounts with respect to those investments. The Advisor and its affiliates intend to allocate investment opportunities to us and Other Advisor Accounts in a manner that they believe in their judgment and based upon their fiduciary duties to be appropriate given the investment objectives, size of transaction, investable assets, alternative investments potentially

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available, prior allocations, liquidity, maturity, expected holding period, diversification, lender covenants and other limitations of ours and the Other Advisor Accounts. See " Risks related to our operations as a BDC While our ability to enter into transactions with our affiliates is restricted under the 1940 Act, we have received an exemptive order from the SEC permitting certain affiliated investments subject to certain conditions. As a result, the Advisor may face conflicts of interests and investments made pursuant to the exemptive order conditions could in certain circumstances adversely affect the price paid or received by us or the availability or size of the position purchased or sold by us."

There may be situations in which Other Advisor Accounts and the Company might invest in different securities issued by the same portfolio company. It is possible that if the portfolio company's financial performance and condition deteriorates such that one or both investments are or could be impaired, the Advisor might face a conflict of interest given the difference in seniority of the respective investments. In such situations, the Advisor would review the conflict on a case-by-case basis and implement procedures consistent with its fiduciary duty to enable it to act fairly to the Other Advisor Accounts and the Company in the circumstances. Any steps by the Advisor will take into consideration the interests of each of the affected clients, the circumstances giving rise to the conflict, the procedural efficacy of various methods of addressing the conflict and applicable legal requirements.

Moreover, the Advisor's investment professionals, its Investment Committee (as defined below), its senior management and employees serve or may serve as officers, directors or principals of entities that operate in the same or a related line of business. Accordingly, these individuals may have obligations to investors in those entities or funds, the fulfillment of which might not be in our best interests or the best interests of our stockholders. In addition, certain of the personnel employed by the Advisor or focused on our business may change in ways that are detrimental to our business.

We have limited operating history as a BDC and, if the Advisor is unable to manage our investments effectively, we may be unable to achieve our investment objective.

Our ability to achieve our investment objective will depend on our ability to manage our business, which will depend, in turn, on the ability of the Advisor to identify, invest in and monitor companies that meet our investment criteria. Accomplishing this result largely will be a function of the Advisor's investment process. Although the Advisor manages closed-end funds with similar restrictions, the 1940 Act imposes numerous constraints on the operations of BDCs. The Advisor's limited experience in operating under these constraints may hinder the Advisor's ability to help us take advantage of attractive investment opportunities and to achieve our investment objectives. For example, BDCs are prohibited from making any nonqualifying investment unless at least 70% of their total assets are primarily in qualifying investments, which are primarily securities of private or thinly-traded U.S. companies (excluding certain financial companies), cash, cash equivalents, U.S. Government securities and other high quality debt investments that mature in one year or less. The Advisor has limited experience investing under these constraints. In addition, the General Partner has limited experience administering a BDC.

The Advisor and its partners, officers, directors, stockholders, members, managers, employees, affiliates and agents may be subject to certain potential or actual conflicts of interest in connection with the activities of, and investments by, us.

The Advisor and its affiliates may spend substantial time on other business activities, including investment management and advisory activities for entities with the same or overlapping investment objectives, investing for their own account, financial advisory services (including services for entities in which we invest), and acting as directors, officers, creditor committee members or in similar capacities. Subject to the requirements of the 1940 Act and other applicable laws, the Advisor and its affiliates and associates intend to engage in such activities and may receive compensation from third parties for their services. Subject to the same requirements, such compensation may be payable by entities in which we invest in connection with actual or contemplated investments, and the Advisor may receive fees and other compensation in connection with structuring investments which they will share.

The Advisor's management fee is based on a percentage of our total assets (other than cash or cash equivalents) and the Advisor may have conflicts of interest in connection with decisions that could affect our total assets, such as decisions as to whether to incur additional debt to increase management fees paid and to recoup the Advisor's payment of half of the sales load in connection with our initial public offering in April 2012.

Our incentive compensation may induce the Advisor to make certain investments, including speculative investments.

The incentive compensation payable by us to the Advisor and the General Partner may create an incentive for the Advisor to make investments on our behalf that are risky or more speculative than would be the case in the absence of such compensation arrangement. The way in which the incentive compensation payable to the Advisor is determined may encourage the Advisor to increase the use of leverage or take additional risk to increase the return on our investments. Under certain circumstances, the use of leverage may increase the likelihood of default, which would disfavor the holders of our common stock, including investors in the offerings pursuant to this prospectus and any related prospectus supplement, or of securities convertible into our common stock or warrants representing rights to purchase our common stock or securities convertible into our common stock. A rise in the general level of interest rates can be expected to lead to higher interest rates applicable to certain of our debt investments and may accordingly result in a substantial increase in the amount of incentive compensation payable to the Advisor with respect to our cumulative investment income. Although the incentive compensation payable to the General Partner or the Advisor is subject to a total return limitation, the Advisor may have some ability to accelerate the realization of gains to obtain incentive compensation earlier than it otherwise would when it may be in our best interests to not yet realize gains. Our directors monitor our use of leverage and the Advisor's management of our investment program in the best interests of our common stockholders.

We may invest, to the extent permitted by law, in the securities and instruments of other investment companies, including private funds, and, to the extent we so invest, we will bear our ratable share of any such investment company's expenses, including management and performance fees. We will also remain obligated to pay management and incentive compensation to the Advisor with respect to the assets invested in the securities and instruments of other investment companies. With respect to each of these investments, each of our common stockholders will bear his or her share of our management and incentive compensation as well as indirectly bear the management and performance fees and other expenses of any investment companies in which we invest.

We may be obligated to pay the Advisor incentive compensation payments in excess of the amounts we would have paid if such compensation was subject to clawback arrangements.

The Advisor or the General Partner is entitled to incentive compensation for each fiscal quarter after January 1, 2013 in an amount equal to a percentage of our ordinary income (before deducting incentive compensation) since that date and, separately, a percentage of our realized capital gains (net of realized capital losses and unrealized depreciation) since that date, in each case subject to a cumulative total return requirement. If we pay incentive compensation and thereafter experience additional realized capital losses or unrealized capital depreciation such that we would no longer have been required to provide incentive compensation, we will not be able to recover any portion of the incentive compensation previously paid or distributed because our incentive compensation arrangements do not contain any clawback provisions. As a result, the incentive compensation could exceed 20% of our cumulative total return, depending on the timing of unrealized appreciation, net unrealized depreciation and net realized capital losses. For example, part of the incentive compensation

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payable or distributable by us that relates to our ordinary income is computed on income that may include interest that has been accrued but not yet received in cash. If a portfolio company defaults on a loan, it is possible that accrued interest previously used in the calculation of the incentive compensation will become uncollectible. Similarly, the income component is measured against a total return limitation that includes unrealized gains. Such gains may not be realized or may be realized at a lower amount. Consequently, we may have paid incentive compensation on income in circumstances where we otherwise would not have done so and with respect to which we do not have a clawback right against the Advisor or the General Partner.

The General Partner may have certain interests that conflict with the interests of the board of directors in the governance of the Operating Company.

The General Partner, an affiliate of the Advisor, is responsible for the day-to-day operations of the Operating Company subject to the general supervision of the board of directors including various significant matters such as the issuance of additional classes of securities of the Operating Company and the determination of the timing and amounts of distributions payable by the Operating Company. The decisions of the General Partner with respect to these and other matters may be subject to various conflicts of interest arising out of its relationship with us and its affiliates. The General Partner could be confronted with decisions where it will, directly or indirectly, have an economic incentive to place its interests or the interests of its affiliates above ours.

The procedures for the appointment and removal of directors from the board of directors of the Operating Company differ from those of the Holding Company, which may result in the boards of directors of the Operating Company and the Holding Company consisting of different members.

The procedures for the appointment and removal of directors from the board of directors of the Operating Company differ from those of the Holding Company, which may result in the boards of directors of the Operating Company and the Holding Company consisting of different members. If the boards of directors of the Operating Company and the Holding Company consist of different members, the objectives of the boards of directors may differ and decisions regarding the management of the Operating Company may adversely affect the Holding Company.

We are dependent upon senior management personnel of the Advisor for our future success, and if the Advisor is unable to retain qualified personnel or if the Advisor loses any member of its senior management team, our ability to achieve our investment objective could be significantly harmed.

The success of the Company is highly dependent on the financial and managerial expertise of the Advisor. The loss of one or more of the voting members of the Investment Committee could have a material adverse effect on the performance of the Company. Although the Advisor and the voting members of the Investment Committee devote a significant amount of their respective efforts to the Company, they actively manage investments for other clients and are not required to (and will not) devote all of their time to the Company's affairs.

The Advisor or its affiliates may, from time to time, possess material non-public information, limiting our investment discretion.

The Advisor's investment professionals, Investment Committee or their respective affiliates may serve as directors of, or in a similar capacity with, companies in which we invest. In the event that material non-public information is obtained with respect to such companies, or we became subject to trading restrictions under the internal trading policies of those companies or as a result of applicable law or regulations, we could be prohibited for a period of time from purchasing or selling the securities of such companies, and this prohibition may have an adverse effect on us and, consequently, your interests as a stockholder.

The Advisor can resign on 60 days' notice, and we may not be able to find a suitable replacement within that time, resulting in a disruption in our operations that could adversely affect our financial condition, business and results of operations.

The Advisor has the right, under our investment management agreement, to resign at any time upon not more than 60 days' written notice, whether we have found a replacement or not. If the Advisor resigns, we may not be able to find a new investment advisor or hire internal management with similar expertise and ability to provide the same or equivalent services on acceptable terms within 60 days, or at all. If we are unable to do so quickly, our operations are likely to experience a disruption, our financial condition, business and results of operations as well as our ability to pay distributions are likely to be adversely affected and the market price of our shares may decline. In addition, the coordination of our internal management and investment activities is likely to suffer if we are unable to identify and reach an agreement with a single institution or group of executives having the expertise possessed by the Advisor and its affiliates. Even if we are able to retain comparable management, whether internal or external, the integration of such management and their lack of familiarity with our investment objective may result in additional costs and time delays that may adversely affect our financial condition, business and results of operations.

We may experience fluctuations in our periodic operating results.

We could experience fluctuations in our periodic operating results due to a number of factors, including the interest rates payable on the debt securities we acquire, the default rate on such securities, the level of our expenses (including the interest rates payable on our borrowings), the dividend rates payable on preferred stock we issue, variations in and the timing of the recognition of realized and unrealized gains or losses, the degree to which we encounter competition in our markets and general economic conditions. As a result of these factors, results for any period should not be relied upon as being indicative of performance in future periods.

If we fail to maintain our status as a business development company, our business and operating flexibility could be significantly reduced.

We qualify as business development companies under the 1940 Act. The 1940 Act imposes numerous constraints on the operations of business development companies. For example, BDCs are prohibited from making any unqualifying investments unless at least 70% of their total assets are invested in qualifying investments which are primarily securities of private or thinly-traded U.S. companies, cash, cash equivalents, U.S. government securities and other high quality debt investments that mature in one year or less. Failure to comply with the requirements imposed on business development companies by the 1940 Act could cause the SEC to bring an enforcement action against us and/or expose us to claims of private litigants. In addition, any such failure could cause an event of default under the Leverage Program, which could have a materially adverse effect on our business, financial conditions or results of operations. See "Regulation."

Because we intend to distribute substantially all of our income to our stockholders to maintain our status as a RIC, we will continue to need additional capital to finance growth. If additional funds are unavailable or not available on favorable terms, our ability to grow will be impaired.

In order for the Holding Company to qualify for the tax benefits available to RICs and to avoid payment of excise taxes, we intend to distribute to our stockholders substantially all of our annual taxable income, except that we may retain certain net capital gains for reinvestment in common interests of the Operating Company, and treat such amounts as deemed distributions to our stockholders. If we elect to treat any amounts as deemed distributions, we must pay income taxes at the corporate rate on such deemed distributions on behalf of our stockholders and our stockholders will receive a tax credit for such amounts and an increase in basis. A stockholder that is not subject to U.S.

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federal income tax or otherwise is not required to file a U.S. federal income tax return would be required to file a U.S. federal income tax return on the appropriate form in order to claim a refund for the taxes we paid. As a result of these requirements, we will likely need to raise capital from other sources to grow our business. Unfavorable economic or capital market conditions may increase our funding costs, limit our access to the capital markets or could result in a decision by lenders not to extend credit to us. An inability to successfully access the capital markets could limit our ability to grow our business and fully execute our business strategy and could decrease our earnings, if any.

As a BDC, we are not able to incur senior securities unless after giving effect thereto we meet a coverage ratio of total assets, less liabilities and indebtedness not represented by senior securities, to total senior securities, which includes all of our borrowings and any outstanding preferred interests, of at least 200%. These requirements limit the amount that we may borrow. Because we will continue to need capital to grow our investment portfolio, these limitations may prevent us from incurring debt and require us to raise additional equity at a time when it may be disadvantageous to do so. While we expect we will be able to borrow and to issue additional debt securities and expect that we will be able to issue additional equity securities, we cannot assure you that debt and equity financing will be available to us on favorable terms, or at all. In addition, as a business development company, we generally will not be permitted to issue equity securities priced below net asset value without stockholder approval. If additional funds are not available to us, we could be forced to curtail or cease new investment activities and our net asset value or common stock price could decline.

The highly competitive market in which we operate may limit our investment opportunities.

A number of entities compete with us to make the types of investments that we make. We compete with other BDCs, public and private funds, commercial and investment banks, commercial financing companies, and, to the extent they provide an alternative form of financing, private equity funds. Additionally, because competition for investment opportunities generally has increased among alternative investment vehicles, such as hedge funds, those entities now invest in areas in which they have not traditionally invested. As a result of these new entrants, competition for investment opportunities intensified over the past several years and may intensify further in the future. Some of our existing and potential competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, many of our competitors are not subject to the regulatory restrictions and valuation requirements that the 1940 Act imposes on us as a BDC and that the Code imposes on us as a RIC. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations. Also, as a result of this existing and potentially increasing competition, we may not be able to take advantage of attractive investment opportunities from time to time, and we can offer no assurance that we will be able to identify and make investments that are consistent with our investment objective.

We do not seek to compete primarily based on the interest rates we offer, and we believe that some of our competitors make loans with interest rates that are comparable to or lower than the rates we offer.

We may lose investment opportunities if we do not match our competitors' pricing, terms and structure. If we match our competitors' pricing, terms and structure, we may experience decreased net interest income and increased risk of credit loss. As a result of operating in such a competitive environment, we may make investments that are on better terms to our portfolio companies than what we may have originally anticipated, which may impact our return on these investments.

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Our board of directors may change our operating policies and strategies without prior notice or stockholder approval.

Our board of directors has the authority to modify or waive our operating policies and strategies without prior notice and without stockholder approval. We cannot predict the effect any changes to our current operating policies and strategies would have on our business, operating results or value of our stock. Nevertheless, the effects could adversely affect our business and impact our ability to make distributions and cause you to lose all or part of your investment.

Risks related to our investments

We cannot assure you that we will be able to successfully deploy the proceeds of offerings within the timeframe we have contemplated.

We currently anticipate that a portion of the net proceeds of future offerings will be invested in accordance with our investment objective within six to twelve months following completion of any such offering. We cannot assure you, however, that we will be able to locate a sufficient number of suitable investment opportunities to allow us to successfully deploy in that timeframe that portion of net proceeds of such future offerings. To the extent we are unable to invest within our contemplated timeframe after the completion of an offering, our investment income, and in turn our results of operations, will likely be adversely affected.

We have not yet identified the portfolio company investments we intend to acquire using the proceeds of the offerings.

We have not yet identified the potential investments for our portfolio that we will purchase following the future offerings pursuant to this prospectus and any related prospectus supplement. The Advisor will select our investments subsequent to the closing of any such offering, and our stockholders will have no input with respect to such investment decisions. These factors increase the uncertainty, and thus the risk, of investing in our shares of common stock.

Our investments may be risky, and you could lose all or part of your investment.

We invest mostly in middle-market companies primarily through leveraged loans.

Risks Associated with middle-market companies. Investing in private middle-market companies involves a number of significant risks, including:

- these companies may have limited financial resources and may be unable to meet their obligations under their debt securities that we hold, which may be accompanied by a deterioration in the value of any collateral;

- they typically have shorter operating histories, narrower product lines and smaller market shares than larger businesses, which tend to render them more vulnerable to competitors' actions and market conditions, as well as general economic downturns;

- they are more likely to depend on the management talents and efforts of a small group of persons; therefore, the death, disability, resignation or termination of one or more of these persons could have a material adverse impact on the portfolio company and, in turn, on us;

- they generally have less predictable operating results, may from time to time be parties to litigation, may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence, and may require substantial additional capital to support their operations, finance expansion or maintain their competitive position;

our executive officers, directors and the Advisor may, in the ordinary course of business, be named as defendants in litigation arising from our investments in the portfolio companies;

changes in laws and regulations, as well as their interpretations, may adversely affect their respective businesses, financial structures or prospects; and

they may have difficulty accessing the capital markets to meet future capital needs.

Little public information exists about private middle-market companies, and we expect to rely on the Advisor's investment professionals to obtain adequate information to evaluate the potential returns from investing in these companies. These companies and their financial information are not subject to the Sarbanes-Oxley Act of 2002 and other rules that govern disclosures and financial controls of public companies. If we are unable to uncover all material information about these companies, we may not make a fully informed investment decision, and we may lose money on our investment.

Lower Credit Quality Obligations. Most of our debt investments are likely to be in lower grade obligations. The lower grade investments in which we invest may be rated below investment grade by one or more nationally-recognized statistical rating agencies at the time of investment or may be unrated but determined by the Advisor to be of comparable quality. Debt securities rated below investment grade are commonly referred to as "junk bonds" and are considered speculative with respect to the issuer's capacity to pay interest and repay principal. The debt that we invest in typically is not initially rated by any rating agency, but we believe that if such investments were rated, they would be below investment grade (rated lower than "Baa3" by Moody's Investors Service, lower than "BBB-" by Fitch Ratings or lower than "BBB-" by Standard & Poor's). We may invest without limit in debt of any rating, as well as debt that has not been rated by any nationally recognized statistical rating organization.

Investment in lower grade investments involves a substantial risk of loss. Lower grade securities or comparable unrated securities are considered predominantly speculative with respect to the issuer's ability to pay interest and principal and are susceptible to default or decline in market value due to adverse economic and business developments. The market values for lower grade debt tend to be very volatile and are less liquid than investment grade securities. For these reasons, your investment in our company is subject to the following specific risks:

increased price sensitivity to a deteriorating economic environment;

greater risk of loss due to default or declining credit quality;

adverse company specific events are more likely to render the issuer unable to make interest and/or principal payments; and

if a negative perception of the lower grade debt market develops, the price and liquidity of lower grade securities may be depressed. This negative perception could last for a significant period of time.

Adverse changes in economic conditions are more likely to lead to a weakened capacity of a lower grade issuer to make principal payments and interest payments than an investment grade issuer. The principal amount of lower grade securities outstanding has proliferated in the past decade as an increasing number of issuers have used lower grade securities for corporate financing. An economic downturn could severely affect the ability of highly leveraged issuers to service their debt obligations or to repay their obligations upon maturity. Similarly, downturns in profitability in specific industries could adversely affect the ability of lower grade issuers in that industry to meet their obligations. The market values of lower grade debt tend to reflect individual developments of the issuer to a greater extent than do higher quality investments, which react primarily to fluctuations in the general level of interest rates. Factors having an adverse impact on the market value of lower grade debt may have an adverse effect on our net asset value and the market value of our common stock. In addition, we may incur additional expenses to the extent we are required to seek recovery upon a default in payment of principal of or interest on our portfolio holdings. In certain circumstances, we may be required to foreclose on an issuer's assets and take possession of its property or operations. In such circumstances, we would incur additional costs in disposing of such assets and potential liabilities from operating any business acquired.

The secondary market for lower grade debt is unlikely to be as liquid as the secondary market for more highly rated debt, a factor which may have an adverse effect on our ability to dispose of a particular instrument. There are fewer dealers in the market for lower grade securities than investment grade obligations. The prices quoted by different dealers may vary significantly and the spread between the bid and asked price is generally larger than for higher quality instruments. Under adverse market or economic conditions, the secondary market for lower grade debt could contract further, independent of any specific adverse changes in the condition of a particular issuer, and these instruments may become highly illiquid. As a result, we could find it more difficult to sell these instruments or may be able to sell the securities only at prices lower than if such instruments were widely traded. Prices realized upon the sale of such lower rated or unrated securities, under these circumstances, may be less than the prices used in calculating our net asset value.

Since investors generally perceive that there are greater risks associated with lower grade debt of the type in which we may invest a portion of our assets, the yields and prices of such debt may tend to fluctuate more than those for higher rated instruments. In the lower quality segments of the fixed income markets, changes in perceptions of issuers' creditworthiness tend to occur more frequently and in a more pronounced manner than do changes in higher quality segments of the income securities market, resulting in greater yield and price volatility.

Distressed Debt Securities Risk. At times, distressed debt obligations may not produce income and may require us to bear certain extraordinary expenses (including legal, accounting, valuation and transaction expenses) in order to protect and recover our investment. Therefore, our ability to achieve current income for our stockholders may be diminished. We also will be subject to significant uncertainty as to when and in what manner and for what value the distressed debt we invest in will eventually be satisfied (e.g., through a liquidation of the obligor's assets, an exchange offer or plan of reorganization involving the distressed debt securities or a payment of some amount in satisfaction of the obligation). In addition, even if an exchange offer is made or plan of reorganization is adopted with respect to distressed debt we hold, there can be no assurance that the securities or other assets received by us in connection with such exchange offer or plan of reorganization will not have a lower value or income potential than may have been anticipated when the investment was made. Moreover, any securities received by us upon completion of an exchange offer or plan of reorganization may be restricted as to resale. As a result of our participation in negotiations with respect to any exchange offer or plan of reorganization with respect to an issuer of distressed debt, we may be restricted from disposing of such securities.

Payment-in-kind Interest Risk. Our loans may contain a payment-in-kind, or PIK, interest provision. PIK investments carry additional risk as holders of these types of securities receive no cash until the cash payment date unless a portion of such securities is sold. If the issuer defaults the Company may obtain no return on its investment. The PIK interest, computed at the contractual rate specified in each loan agreement, is added to the principal balance of the loan and recorded as interest income. To avoid the imposition of corporate-level tax on us, this non-cash source of income needs to be paid out to stockholders in cash distributions or, in the event that we determine to do so and in certain cases, in shares of our common stock, even though we have not yet collected and may never collect the cash relating to the PIK interest. As a result, we may have to distribute a taxable stock dividend to account for PIK interest even though we have not yet collected the cash.

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Preferred Stock Risk. To the extent we invest in preferred securities, there are special risks, including:

Deferral. Preferred securities may include provisions that permit the issuer, at its discretion, to defer distributions for a stated period without any adverse consequences to the issuer. If we own a preferred security that is deferring its distributions, we may be required to report income for tax purposes although we have not yet received such income.

Subordination. Preferred securities are subordinated to bonds and other debt instruments in a company's capital structure in terms of priority to corporate income and liquidation payments, and therefore will be subject to greater credit risk than more senior debt instruments.

Liquidity. Preferred securities may be substantially less liquid than many other securities, such as common stocks or U.S. Government securities.

Limited Voting Rights. Generally, preferred security holders have no voting rights with respect to the issuing company unless preferred dividends have been in arrears for a specified number of periods, at which time the preferred security holders may elect a number of directors to the issuer's board. Generally, once all the arrearages have been paid, the preferred security holders no longer have voting rights.

Equity Security Risk. We may have exposure to equity securities. Although equity securities have historically generated higher average total returns than fixed-income securities over the long term, equity securities also have experienced significantly more volatility in those returns. The equity securities that we acquire may fail to appreciate and may decline in value or become worthless.

Hedging Transactions. We may employ hedging techniques to minimize currency exchange rate risks or interest rate risks, but we can offer no assurance that such strategies will be effective. If we engage in hedging transactions, we may expose ourselves to risks associated with such transactions. Hedging against a decline in the values of our portfolio positions does not eliminate the possibility of fluctuations in the values of such positions or prevent losses if the values of such positions decline. Moreover, it may not be possible to hedge against an exchange rate or interest rate fluctuation that is so generally anticipated that we are not able to enter into a hedging transaction at an acceptable price. Additionally, engaging in certain hedging transactions could result in adverse tax consequences, e.g. giving rise to income that does not qualify for the 90% annual gross income requirement applicable to RICs.

Economic recessions or downturns could impair our portfolio companies and harm our operating results.

Over the past several years, the U.S. had been in a prolonged recessionary period followed by slower than historical rates of GDP growth, and it may return to a recessionary period or remain in a period of slow growth. Many other economies are currently in or slowly emerging from a prolonged recessionary period. Although these conditions have ameliorated to some extent, they could continue for a prolonged period of time or worsen in the future. In addition, several EU countries continue to face budget issues, some of which may have negative long-term effects for the economies of those countries and other EU countries. Economic slowdowns or recessions could lead to financial losses in our portfolio and a decrease in revenues, net income and assets. Unfavorable economic conditions also could increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us. These events could prevent us from increasing investments and harm our operating results.

A portfolio company's failure to satisfy financial or operating covenants imposed by us or other lenders could lead to defaults and, potentially, termination of its loans and foreclosure on its secured assets, which could trigger cross-defaults under other agreements and jeopardize our portfolio company's ability to meet its obligations under the debt securities that we hold. We may incur expenses to the extent necessary to seek recovery upon default or to negotiate new terms with a defaulting portfolio company. In addition, if one of our portfolio companies were to go bankrupt, even though we or one of our affiliates may have structured our interest in such portfolio company as senior debt, depending on the facts and circumstances, including the extent to which we actually provided managerial assistance to that portfolio company, a bankruptcy court might re-characterize our debt holding as equity and subordinate all or a portion of our claim to claims of other creditors.

We may not be in a position to exercise control over our portfolio companies or to prevent decisions by management of our portfolio companies that could decrease the value of our investments.

We do not generally intend to take controlling equity positions in our portfolio companies. To the extent that we do not hold a controlling equity interest in a portfolio company, we are subject to the risk that such portfolio company may make business decisions with which we disagree, and the stockholders and management of such portfolio company may take risks or otherwise act in ways that are adverse to our interests. Due to the lack of liquidity for the debt and equity investments that we typically hold in our portfolio companies, we may not be able to dispose of our investments in the event we disagree with the actions of a portfolio company, and may therefore suffer a decrease in the value of our investments.

In addition, we may not be in a position to control any portfolio company by investing in its debt securities. As a result, we are subject to the risk that a portfolio company in which we invest may make business decisions with which we disagree and the management of such company, as representatives of the holders of their common equity, may take risks or otherwise act in ways that do not serve our interests as debt investors.

Our portfolio companies may incur debt that ranks equally with, or senior to, our investments in such companies.

The portfolio companies we invest in usually have, or may be permitted to incur, other debt that ranks equally with, or senior to, the debt securities in which we invest. By their terms, such debt instruments may provide that the holders are entitled to receive payment of interest or principal on or before the dates on which we are entitled to receive payments in respect of the debt securities in which we invest. Also, in the event of insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company, holders of debt instruments ranking senior to our investment in that portfolio company would typically be entitled to receive payment in full before we receive any distribution in respect of our investment. After repaying such senior creditors, such portfolio company may not have any remaining assets to use for repaying its obligation to us. In the case of debt ranking equally with debt securities in which we invest, we would have to share any distributions on an equal and ratable basis with other creditors holding such debt in the event of an insolvency, liquidation, dissolution, reorganization or bankruptcy of the relevant portfolio company.

Additionally, certain loans that we make to portfolio companies may be secured on a second priority basis by the same collateral securing senior secured debt of such companies. The first priority liens on the collateral will secure the portfolio company's obligations under any outstanding senior debt and may secure certain other future debt that may be permitted to be incurred by the portfolio company under the agreements governing the loans. The holders of obligations secured by the first priority liens on the collateral will generally control the liquidation of and be entitled to receive proceeds from any realization of the collateral to repay their obligations in full before us. In addition, the value of the collateral in the event of liquidation will depend on market and economic conditions, the availability of buyers and other factors. There can be no assurance that the proceeds, if any, from the sale or sales of all of the collateral would be sufficient to satisfy the loan obligations secured by the second priority liens after payment in full of all obligations secured by the first priority liens on the

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collateral. If such proceeds are not sufficient to repay amounts outstanding under the loan obligations secured by the second priority liens, then we, to the extent not repaid from the proceeds of the sale of the collateral, will only have an unsecured claim against the portfolio company's remaining assets, if any.

The rights we may have with respect to the collateral securing the loans we make to our portfolio companies with senior debt outstanding may also be limited pursuant to the terms of one or more intercreditor agreements that we enter into with the holders of senior debt. Under such an intercreditor agreement, at any time that obligations that have the benefit of the first priority liens are outstanding, any of the following actions that may be taken in respect of the collateral will be at the direction of the holders of the obligations secured by the first priority liens: the ability to cause the commencement of enforcement proceedings against the collateral; the ability to control the conduct of such proceedings; the approval of amendments to collateral documents; releases of liens on the collateral; and waivers of past defaults under collateral documents. We may not have the ability to control or direct such actions, even if our rights are adversely affected.

We may also make unsecured loans to portfolio companies, meaning that such loans will not benefit from any interest in collateral of such companies. Liens on such portfolio companies' collateral, if any, will secure the portfolio company's obligations under its outstanding secured debt and may secure certain future debt that is permitted to be incurred by the portfolio company under its secured loan agreements. The holders of obligations secured by such liens will generally control the liquidation of, and be entitled to receive proceeds from, any realization of such collateral to repay their obligations in full before us. In addition, the value of such collateral in the event of liquidation will depend on market and economic conditions, the availability of buyers and other factors. There can be no assurance that the proceeds, if any, from sales of such collateral would be sufficient to satisfy our unsecured loan obligations after payment in full of all secured loan obligations. If such proceeds were not sufficient to repay the outstanding secured loan obligations, then our unsecured claims would rank equally with the unpaid portion of such secured creditors' claims against the portfolio company's remaining assets, if any.

Our portfolio companies may prepay loans, which prepayment may reduce stated yields in the future if capital returned cannot be invested in transactions with equal or greater expected yields.

Certain of the loans we make are prepayable at any time, some of them of them at no premium to par. We cannot predict when such loans may be prepaid. Whether a loan is prepaid will depend both on the continued positive performance of the portfolio company and the existence of favorable financing market conditions that permit such company to replace existing financing with less expensive capital. As market conditions change frequently, it is unknown when, and if, this may be possible for each portfolio company. In the case of some of these loans, having the loan prepaid early may reduce the achievable yield for the Company in the future below the current yield disclosed for our portfolio if the capital returned cannot be invested in transactions with equal or greater expected yields.

Our failure to make follow-on investments in our portfolio companies could impair the value of our portfolio.

Following an initial investment in a portfolio company, we may make additional investments in that portfolio company as "follow-on" investments in order to: (1) increase or maintain in whole or in part our equity ownership percentage; (2) exercise warrants, options or convertible securities that were acquired in the original or subsequent financing; or (3) attempt to preserve or enhance the value of our initial investment.

We may elect not to make follow-on investments or otherwise lack sufficient funds to make those investments. Our failure to make follow-on investments may, in some circumstances, jeopardize the continued viability of a portfolio company and our initial investment, or may result in a missed opportunity for us to increase our participation in a successful operation. Even if we have sufficient capital to make a desired follow-on investment, we may elect not to make such follow-on investment because we may not want to increase our concentration of risk, because we prefer other opportunities, because we are inhibited by compliance with BDC requirements or because we desire to maintain our tax status.

Our investments in foreign securities may involve significant risks in addition to the risks inherent in U.S. investments.

Our investment strategy contemplates that a portion of our investments may be in securities of foreign companies in order to provide diversification or to complement our U.S. investments, although we are required generally to invest at least 70% of our assets in companies organized and having their principal place of business within the U.S. and its possessions. Investing in foreign companies may expose us to additional risks not typically associated with investing in U.S. companies. These risks include changes in exchange control regulations, political and social instability, expropriation, imposition of foreign taxes, less liquid markets and less available information than is generally the case in the United States, higher transaction costs, less government supervision of exchanges, brokers and issuers, less developed bankruptcy laws, difficulty in enforcing contractual obligations, lack of uniform accounting and auditing standards and greater price volatility. These risks may be more pronounced for portfolio companies located or operating primarily in emerging markets, whose economies, markets and legal systems may be less developed.

Although it is anticipated that most of our investments will be denominated in U.S. dollars, our investments that are denominated in a foreign currency will be subject to the risk that the value of a particular currency may change in relation to the U.S. dollar. Among the factors that may affect currency values are trade balances, the level of short-term interest rates, differences in relative values of similar assets in different currencies, long-term opportunities for investment and capital appreciation and political developments. We may employ hedging techniques to minimize these risks, but we can offer no assurance that we will, in fact, hedge currency risk or, that if we do, such strategies will be effective. As a result, a change in currency exchange rates may adversely affect our profitability.

Risks related to our operations as a BDC

While our ability to enter into transactions with our affiliates is restricted under the 1940 Act, we have received an exemptive order from the SEC permitting certain affiliated investments subject to certain conditions. As a result, the Advisor may face conflicts of interests and investments made pursuant to the exemptive order conditions could in certain circumstances adversely affect the price paid or received by us or the availability or size of the position purchased or sold by us.

Any person that owns, directly or indirectly, 5% or more of our outstanding voting securities or is managed by the Advisor will generally be our affiliate for purposes of the 1940 Act and we are generally prohibited from participating in certain transactions such as co-investing with, or buying or selling any security from or to, such affiliate, absent the prior approval of our independent directors and, in some cases, of the SEC. However, the Advisor and the funds managed by the Advisor have received an exemption from certain SEC regulations prohibiting transactions with affiliates. The exemptive order requires that certain procedures be followed prior to making an investment subject to the order and such procedures could in certain circumstances adversely affect the price paid or received by us or the availability or size of the position purchased or sold by us. The Advisor may also face conflicts of interest in making investments pursuant to the exemptive order. See "Management of the Company Exemptive Order" and " Risks related to our business We have limited operating history as a BDC, and if the Advisor is unable to manage our investments effectively, we may be unable to achieve our investment objective. In addition, the Advisor may face conflicts in allocating investment opportunities between us and certain other entities that could impact our investment returns."

The 1940 Act also prohibits certain "joint" transactions with certain of our affiliates, which could include investments in the same portfolio company (whether at the same or different times), without prior approval of our independent directors and, in some cases, of the SEC. We are prohibited from buying or selling any security from or to any person who owns more than 25% of our voting securities and from or to certain of that person's affiliates, or entering into prohibited joint transactions with such persons, absent the prior approval of the SEC (other than certain limited situations pursuant to current regulatory guidance). The analysis of whether a particular transaction constitutes a joint transaction requires a review of the relevant facts and circumstances relating to the particular transaction. Similar restrictions limit our ability to transact business with our officers or directors or their affiliates.

Regulations governing our operation as a BDC may limit our ability to, and the way in which we, raise additional capital, which could have a material adverse impact on our liquidity, financial condition and results of operations.

Our business may in the future require a substantial amount of capital in addition to the proceeds of these offerings. We may acquire additional capital from the issuance of additional shares of our common stock or from the additional issuance of senior securities (including debt and preferred stock). However, we may not be able to raise additional capital in the future on favorable terms or at all.

Our board of directors may decide to issue common stock to finance our operations rather than issuing debt or other senior securities. As a BDC, we are generally not able to issue our common stock at a price below net asset value without first obtaining required approvals from our stockholders and our independent directors. If our common stock trades at a discount to net asset value, those restrictions could adversely affect our ability to raise equity capital. Except in connection with the exercise of warrants or the conversion of convertible securities, in any such case the price at which our securities are to be issued and sold may not be less than a price, that in the determination of our board of directors, closely approximates the market value of such securities at the relevant time. We may also make rights offerings to our stockholders at prices per share less than the net asset value per share, subject to the requirements of the 1940 Act. If we raise additional funds by issuing more common stock or senior securities convertible into, or exchangeable for, our common stock, the percentage ownership of our stockholders at that time would decrease, and such stockholders may experience dilution.

We may only issue senior securities up to the maximum amount permitted by the 1940 Act. The 1940 Act permits us to issue senior securities only in amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such issuance or incurrence. If our assets decline in value and we fail to satisfy this test or any stricter test under the terms of our leverage instruments, we may be required to liquidate a portion of our investments and repay a portion of our indebtedness at a time when such sales or repayment may be disadvantageous, which could have a material adverse impact on our liquidity, financial condition and results of operations.

Changes in the laws or regulations governing our business or the business of our portfolio companies, or changes in the interpretations thereof or newly enacted legislation and regulations, and any failure by us or our portfolio companies to comply with these laws or regulations, could have a material adverse effect on our business, results of operations or financial condition of us or our portfolio companies.

We are subject to changing rules and regulations of federal and state governments, as well as the stock exchange in which our common stock is listed. These entities, including the Public Company Accounting Oversight Board, the SEC and The Nasdaq Global Select Market, have issued a significant number of new and increasingly complex requirements and regulations over the course of the last several years and continue to develop additional regulations. Changes in the laws or regulations or the interpretations of the laws and regulations that govern BDCs, RICs or non-depository commercial lenders could significantly affect our operations and our cost of doing business. We are subject to federal, state and local laws and regulations and are subject to judicial and administrative decisions that affect our operations, including our loan originations, maximum interest rates, fees and other charges, disclosures to portfolio companies, the terms of secured transactions, collection and foreclosure procedures and other trade practices. If these laws, regulations or decisions change, or if we expand our business into jurisdictions that have adopted more stringent requirements than those in which we currently conduct business, we may have to incur significant expenses in order to comply, or we might have to restrict our operations. In addition, if we do not comply with applicable laws, regulations and decisions, we may lose licenses needed for the conduct of our business and may be subject to civil fines and criminal penalties, any of which could have a material adverse effect upon our business, results of operations or financial condition.

On July 21, 2010, President Obama signed into law the Dodd-Frank Act. Many of the provisions of the Dodd-Frank Act have extended implementation periods and delayed effective dates and will require extensive rulemaking by regulatory authorities. While the impact of the Dodd-Frank Act on us and our portfolio companies may not be known for an extended period of time, the Dodd-Frank Act, including future rules implementing its provisions and the interpretation of those rules, along with other legislative and regulatory proposals directed at the financial services industry or affecting taxation that are proposed or pending in the U.S. Congress, may negatively impact the operations, cash flows or financial condition of us or our portfolio companies, impose additional costs on us or our portfolio companies, intensify the regulatory supervision of us or our portfolio companies or otherwise adversely affect our business or the business of our portfolio companies.

If we do not invest a sufficient portion of our assets in qualifying assets, we could be precluded from investing in certain assets or could be required to dispose of certain assets, which could have a material adverse effect on our business, financial condition and results of operations.

As a BDC, we are prohibited from acquiring any assets other than "qualifying assets" unless, at the time of and after giving effect to such acquisition, at least 70% of our total assets are qualifying assets. As of September 30, 2013, approximately $54.0 million, or approximately 7.4%, of our total assets were not "qualifying assets." If we do not invest a sufficient portion of our assets in qualifying assets, we will be prohibited from investing in additional non-qualifying assets, which could have a material adverse effect on our business, financial condition and results of operations. Similarly, these rules could prevent us from making follow-on investments in existing portfolio companies (which could result in the dilution of our position) or could require us to dispose of investments at inopportune times in order to come into compliance with the 1940 Act. If we need to dispose of these investments quickly, it may be difficult to dispose of such investments on favorable terms. For example, we may have difficulty in finding a buyer and, even if a buyer is found, we may have to sell the investments at a substantial loss.

We will be subject to corporate-level U.S. federal income tax on all of our income if we are unable to qualify as a RIC under the Code, which would have a material adverse effect on our financial performance.

Although we are currently qualified as a RIC, no assurance can be given that we will be able to maintain RIC status. To maintain RIC status and be relieved of U.S. federal income taxes on income and gains distributed to its stockholders, we generally must meet the annual distribution, source-of-income and asset diversification requirements described below. In addition, our Leverage Program prohibits us from making distributions if doing so causes us to fail to maintain the asset coverage ratios stipulated by the 1940 Act or the Leverage Program.

To qualify as a RIC under the Code, we generally must meet certain source-of-income, asset diversification and annual distribution requirements. The annual distribution requirement for a RIC is

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satisfied if we distribute at least 90% of our ordinary income and net short-term capital gain in excess of net long-term capital loss, if any, to our stockholders. Since we use debt financing and have Preferred Interests outstanding, we are subject to certain asset coverage ratio requirements and other financial covenants under the terms of the Leverage Program, and we are, in some circumstances, also subject to similar requirements under the 1940 Act. The requirements could, under certain circumstances, restrict us from making distributions necessary to qualify as a RIC. If we are unable to obtain cash from other sources, we may fail to qualify as a RIC and, thus, may be subject to corporate-level income tax. To qualify as a RIC, we generally must also meet certain asset diversification requirements at the end of each calendar quarter. Failure to meet these tests may result in our having to dispose of certain investments quickly in order to prevent the loss of RIC status. Because we anticipate that most of our investments will be in private companies, any such dispositions could be made at disadvantageous prices and may result in substantial losses.

If we fail to qualify as a RIC for any reason and become subject to corporate-level income tax, the resulting corporate-level income taxes could substantially reduce our net assets, the amount of income available for distribution and the amount of our distributions. For additional discussion regarding the tax implications of a RIC, see "U.S. Federal Income Tax Matters."

We may have difficulty paying our required distributions if we recognize income before or without receiving cash representing such income.

For U.S. federal income tax purposes, we may include in income certain amounts that we have not yet received in cash, such as original issue discount, which may arise if we receive warrants in connection with the making of a loan or possibly in other circumstances, or PIK interest, which represents contractual interest added to the loan balance and due in the future, often only at the end of the loan. Such original issue discount, which could be significant relative to our overall investment activities, or increases in loan balances as a result of PIK arrangements are generally included in our taxable income before we receive any corresponding cash payments. We also may be required to include in income certain other amounts that we do not receive in cash.

Since we may recognize taxable income before or without receiving cash representing such income, if we invest to a substantial extent in non-cash paying debt instruments we may have difficulty meeting the tax requirement to distribute at least 90% of our ordinary income and net short-term capital gain in excess of net long-term capital loss, if any, to maintain our status as a RIC. Accordingly, we may have to sell some of our investments at times we would not consider advantageous, raise additional debt or equity capital or reduce new investment originations to meet these distribution requirements.

There is a risk that you may not receive distributions or that our distributions may not grow over time and a portion of our distributions may be a return of capital.

We intend to make distributions on a quarterly basis to our stockholders out of assets legally available for distribution. We cannot assure you that we will achieve investment results that will allow us to make a specified level of cash distributions or year-to-year increases in cash distributions. Our ability to pay distributions might be adversely affected by the impact of one or more of the risk factors described in this prospectus. Due to the asset coverage test applicable to us under the 1940 Act as a BDC, we may be limited in our ability to make distributions.

Efforts to comply with Section 404 of the Sarbanes-Oxley Act involve significant expenditures, and non-compliance with Section 404 of the Sarbanes-Oxley Act may adversely affect us and the market price of our common stock.

Under current SEC rules, we are required to report on our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act and related rules and regulations of the

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SEC. We are required to review on an annual basis our internal control over financial reporting, and on a quarterly and annual basis to evaluate and disclose changes in our internal control over financial reporting. As a result, we are incurring additional expenses that may negatively impact our financial performance and our ability to make distributions. This process results in a diversion of management's time and attention. We cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations, and we may not be able to ensure that the process is effective or that our internal control over financial reporting is or will be effective in a timely manner. In the event that we are unable to maintain or achieve compliance with Section 404 of the Sarbanes-Oxley Act and related rules, we and the market price of our common stock may be adversely affected.

Risks relating to the offerings pursuant to this prospectus

We may use proceeds of future offerings in a way with which you may not agree.

We will have significant flexibility in applying the proceeds of the offerings and may use the net proceeds from the offerings in ways with which you may not agree, or for purposes other than those contemplated at the time of such offerings. We will also pay operating expenses, and may pay other expenses such as due diligence expenses of potential new investments, from the net proceeds of future offerings. Our ability to achieve our investment objective may be limited to the extent that net proceeds of such offerings, pending full investment, are used to pay expenses rather than to make investments.

If we incur additional leverage, it will increase the risk of investing in shares of our common stock.

The Company has indebtedness and the Preferred Interests outstanding pursuant to the Leverage Program and expects, in the future, to borrow additional amounts under the Revolving Facilities and may increase the size of the Revolving Facilities or enter into other borrowing arrangements. The Company's portfolio must experience an annual return of 0.73% in order to cover annual interest and dividend payments under the Leverage Program as of September 30, 2013.

Illustration. The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns, net of expenses and preferred dividends. The calculations in the table below are hypothetical and actual returns may be higher or lower than those appearing below. The calculation is based on our level of leverage at September 30, 2013, which represented borrowings and preferred stock equal to 38.9% of our total assets. On such date, we also had $729.3 million in total assets; an average cost of funds of 1.22%; $284.0 million aggregate principal amount of debt and liquidation preference of the Preferred Interests outstanding; and $401.5 million of total net assets. In order to compute the "Corresponding Return to Common Stockholders," the "Assumed Return on Portfolio (Net of Expenses Other than Interest)" is multiplied by the total value of our investment portfolio at September 30, 2013 to obtain an assumed return to us. From this amount, the interest expense and preferred dividends calculated by multiplying the blended interest and dividend rate of 1.22% by the $284.0 million of debt and preferred stock is subtracted to determine the return available to common stockholders. The return available to common stockholders is then divided by the total value of our net assets at September 30, 2013 to determine the "Corresponding Return to Common Stockholders." Actual interest payments and preferred dividends may be different.

Assumed Return on Portfolio (Net of Expenses Other than Interest and Preferred Dividends)	**-10%**	**-5%**	**0%**	**5%**	**10%**
Corresponding Return to Common Stockholders	-19%	-10%	-1%	8%	17%

The assumed portfolio return in the table is based on SEC regulations and is not a prediction of, and does not represent, our projected or actual performance. The table also assumes that we will maintain a constant level of leverage. The amount of leverage that we use will vary from time to time.

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Our most recent NAV was calculated as of September 30, 2013 and our NAV when calculated as of any date thereafter may be higher or lower.

Our most recently estimated NAV per share is $15.06 determined by us as of September 30, 2013. NAV per share as of December 31, 2013, may be higher or lower than $15.06 based on potential changes in valuations, issuances of securities and earnings for the quarter then ended. Our board of directors has not yet determined the fair value of portfolio investments as of any date subsequent to September 30, 2013. Our board of directors determines the fair value of our portfolio investments on a quarterly basis in connection with the preparation of quarterly financial statements and based on input from independent valuation firms, the Advisor, the Administrator and the audit committee of our board of directors.

Shares of our common stock may trade at a discount to our net asset value per share.

Common stock of BDCs, like that of closed-end investment companies, frequently trades at a discount to current net asset value, which could adversely affect the ability to raise capital. In the past, shares of our common stock have traded at a discount to our net asset value. The risk that shares of our common stock may continue to trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline.

If we sell shares of our common stock at a discount to our net asset value per share, stockholders who do not participate in such sale will experience immediate dilution in an amount that may be material.

The issuance or sale by us of shares of our common stock at a discount to net asset value poses a risk of dilution to our stockholders. In particular, stockholders who do not purchase additional shares of common stock at or below the discounted price in proportion to their current ownership will experience an immediate decrease in net asset value per share (as well as in the aggregate net asset value of their shares of common stock if they do not participate at all). These stockholders will also experience a disproportionately greater decrease in their participation in our earnings and assets and their voting power than the increase we experience in our assets, potential earning power and voting interests from such issuance or sale. In addition, such sales may adversely affect the price at which our common stock trades. For additional information and hypothetical examples of these risks, see "Description of Securities Sales of Common Stock Below Net Asset Value" and the prospectus supplement pursuant to which such sale is made.

Your interest in us may be diluted if you do not fully acquire your proportionate share of any warrants, options or other rights to subscribe for, convert to, or purchase our common stock that we sell. In addition, in such circumstances, if the price at which we sell such warrants, options or other rights to subscribe for, convert to, or purchase our common stock, together with the exercise price, is less than our net asset value per share, then you will experience dilution of the net asset value of your shares.

Although we are only offering shares of our common stock pursuant to this prospectus, we received authority from our stockholders at our 2013 annual meeting to issue warrants, options or other rights to subscribe for, convert to, or purchase shares of our common stock, which may include convertible preferred stock and convertible debentures. In the event we issue warrants, options or other rights to subscribe for, convert into, or purchase our common stock, stockholders who do not acquire such rights will own a smaller proportional interest in us than would otherwise be the case. We cannot state precisely the amount of any such dilution in share ownership because we have no current intention of making any such offering and do not know at this time the terms or amount of such rights.

In addition, if the price at which we sell such warrants, options or other rights to subscribe for, convert to, or purchase our common stock, together with the exercise price, is less than the net asset value per share of our common stock, then our stockholders who do not acquire their proportionate share of such rights will experience dilution of the aggregate net asset value of their shares as a result of the offering. The amount of any such decrease in net asset value is not predictable because it is not known at this time what the price of the warrants, options or other rights to subscribe for, convert into, or purchase our common stock and net asset value per share will be. In the event we issue warrants, options or other rights to subscribe for, convert into, or purchase our common stock, stockholders who do not acquire such rights will own a smaller proportional interest in us than would otherwise be the case. We cannot state precisely the amount of any such dilution in share ownership because we have no current intention of making any such offering and do not know at this time the terms or amount of such rights.

In addition, if the price at which we sell such warrants, options or other rights to subscribe for, convert to, or purchase our common stock, together with the exercise price, is less than the net asset value per share of our common stock, then our stockholders who do not acquire their proportionate share of such rights will experience dilution of the aggregate net asset value of their shares as a result of the offering. The amount of any such decrease in net asset value is not predictable because it is not known at this time what the price of the warrants, options or other rights to subscribe for, convert into, or purchase our common stock and net asset value per share will be.

Our common stock price may be volatile and may fluctuate substantially.

As with any stock, the price of our common stock will fluctuate with market conditions and other factors. If you sell shares, the price received may be more or less than the original investment. Net asset value will be reduced immediately following our offering by the amount of the sales load and selling expenses paid by us. At our 2013 annual meeting of stockholders held on May 1, 2013, our stockholders approved our ability, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering, to sell shares of our common stock at any level of discount from net asset value per share during the 12 month period following the date of the meeting. It should be noted that, theoretically, we may offer up to 25% of our then outstanding common stock each day. Our common stock is intended for long-term investors and should not be treated as a trading vehicle. Shares of BDCs and closed-end management investment companies, which are structured similarly to us, frequently trade at a discount from their net asset value. This characteristic of closed-end investment companies is separate and distinct from the risk that our net asset value per share of common stock may decline. We cannot predict whether our common stock will trade at, above or below net asset value. This risk of loss associated with this characteristic of BDCs and closed-end management investment companies may be greater for investors who sell their shares in a relatively short period of time after completion of an offering.

The market price of our common stock may fluctuate significantly.

The market price and liquidity of the market for our common stock may be significantly affected by numerous factors, some of which are beyond our control and may not be directly related to our operating performance. These factors include:

- significant volatility in the market price and trading volume of securities of BDCs or other companies in the sector in which we operate, which are not necessarily related to the operating performance of these companies;
- price and volume fluctuations in the overall stock market from time to time;
- changes in law, regulatory policies or tax guidelines, particularly with respect to RICs or BDCs;
- loss of RIC status;
- changes in earnings or variations in operating results;

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- changes in the value of our portfolio of investments;
- any shortfall in revenue or net income or any increase in losses from levels expected by investors or securities analysts;
- departure of key personnel from the Advisor;
- operating performance of companies comparable to us;
- short-selling pressure with respect to shares of our common stock or BDCs generally;
- uncertainty surrounding the strength of the U.S. economic recovery;
- general economic trends and other external factors; and
- loss of a major funding source.

There is a risk that investors in our common stock may not receive dividends or that our dividends may not grow over time and investors in our debt securities may not receive all of the interest income to which they are entitled.

We intend to make distributions on a quarterly basis to our stockholders out of assets legally available for distribution. We cannot assure you that we will achieve investment results that will allow us to make a specified level of cash distributions or year-to-year increases in cash distributions. If we declare a dividend and if more stockholders opt to receive cash distributions rather than participate in our dividend reinvestment plan, we may be forced to sell some of our investments in order to make cash dividend payments.

In addition, due to the asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions. Further, if we invest a greater amount of assets in equity securities that do not pay current dividends, it could reduce the amount available for distribution.

The above-referenced restrictions on distributions may also inhibit our ability to make required interest payments to holders of our debt, which may cause a default under the terms of our debt agreements. Such a default could materially increase our cost of raising capital, as well as cause us to incur penalties under the terms of our debt agreements.

Investing in our common stock may involve a high degree of risk and is highly speculative.

The investments we make in accordance with our investment objective may result in a higher amount of risk than alternative investment options and volatility or loss of principal. Our investments in portfolio companies may be speculative and aggressive, and therefore, an investment in our shares may not be suitable for someone with low risk tolerance.

Stockholders may experience dilution in their ownership percentage if they do not participate in our dividend reinvestment plan.

Our dividends are generally declared in cash and stockholders must "opt in" to our dividend reinvestment plan if they want such shares to be automatically reinvested in shares of our common stock. As a result, our stockholders that do not opt in to our dividend reinvestment plan will experience dilution to their ownership percentage of our common stock over time.

Certain provisions of the Delaware General Corporation Law and our certificate of incorporation and bylaws and certain aspects of our structure could deter takeover attempts and have an adverse impact on the price of our common stock.

The Delaware General Corporation Law, our certificate of incorporation and our bylaws contain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. These anti-takeover provisions may inhibit a change in control in circumstances that could give

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the holders of our common stock the opportunity to realize a premium over the market price of our common stock.

For example, to convert us to a closed-end or open-end investment company, to merge or consolidate us with any entity or sell all or substantially all of our assets to any entity in a transaction as a result of which the governing documents of the surviving entity do not contain substantially the same anti-takeover provisions as are provided in our certificate of incorporation or to liquidate and dissolve us other than in connection with a qualifying merger, consolidation or sale of assets or to amend certain of the provisions relating to these matters, our certificate of incorporation requires either (i) the favorable vote of a majority of our continuing directors followed by the favorable vote of the holders of a majority of our then outstanding shares of each affected class or series of our shares, voting separately as a class or series or (ii) the favorable vote of at least 80% of the then outstanding shares of our capital stock, voting together as a single class.

In addition, the board of directors of the Operating Company is appointed by different procedures than the board of the Holding Company, which could lead to the boards of directors of the Operating Company and the Holding Company having different compositions. Such a difference in composition may further hinder or delay an acquisition proposal.

Our stockholders may receive shares of our common stock as dividends, which could result in adverse tax consequences to stockholders.

In order to satisfy the annual distribution requirement applicable to RICs, we have the ability to declare a large portion of a dividend in shares of our common stock instead of in cash. As long as a portion of such dividend is paid in cash (which portion can be as low as 10% for dividends paid on or before December 31, 2012 with respect to any taxable year ending on or before December 31, 2011) and certain requirements are met, the entire distribution would be treated as a dividend for U.S. federal income tax purposes. As a result, a stockholder would be taxed on 100% of the dividend in the same manner as a cash dividend, even though most of the dividend was paid in shares of our common stock.

Sales of substantial amounts of our common stock in the public market may have an adverse effect on the market price of our common stock.

Sales of substantial amounts of our common stock, or the availability of such common stock for sale, could adversely affect the prevailing market prices for our common stock. If this occurs and continues, it could impair our ability to raise additional capital through the sale of securities should we desire to do so.

Future transactions and these offerings may limit our ability to use our capital loss carryforwards.

We have capital loss carryforwards for U.S. federal income tax purposes. Subject to certain limitations, capital loss carryforwards may be used to offset future recognized capital gains. Section 382 of the Code imposes an annual limitation on the ability of a corporation, including a RIC, that undergoes an "ownership change" to use its capital loss carryforwards. Generally, an ownership change occurs if certain five percent shareholders and public groups increase their ownership in us by 50 percent or more during a three-year period. We do not expect that the offerings will result in an ownership change for Section 382 purposes. However, the offerings will make it more likely that future transactions involving our common stock, including transfers by existing shareholders, could result in such an ownership change. Accordingly, there can be no assurance that an ownership change limiting our ability to use our capital loss carryforwards (and built-in, unrecognized losses, if any) will not occur in the future. Such a limitation would, for any given year, have the effect of potentially increasing the amount of our U.S. federal net capital gains for such year and, hence, the amount of capital gains dividends we would need to distribute to remain a RIC and to avoid U.S. income and excise tax liability.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

In addition to factors previously identified elsewhere in this prospectus, including the "Risks" section of this prospectus, the following factors, among others, could cause actual results to differ materially from forward-looking statements or historical performance:

- the introduction, withdrawal, success and timing of business initiatives and strategies;
- changes in political, economic or industry conditions, the interest rate environment or financial and capital markets, which could result in changes in the value of our assets;
- the valuation of our investments in portfolio companies, particularly those having no liquid trading market;
- the relative and absolute investment performance and operations of the Advisor;
- the impact of increased competition;
- the impact of future acquisitions and divestitures;
- the unfavorable resolution of legal proceedings;
- our business prospects and the financial condition and prospects of our portfolio companies;
- the adequacy of our cash resources and working capital;
- the timing of cash flows, if any, from the operations of our portfolio companies;
- the impact of legislative and regulatory actions and reforms and regulatory, supervisory or enforcement actions of government agencies relating to us, the Advisor or our portfolio companies;
- the ability of the Advisor to identify suitable investments for us and to monitor and administer our investments;
- our contractual arrangements and relationships with third parties;
- any future financings and investments by us;
- the ability of the Advisor to attract and retain highly talented professionals;

- fluctuations in interest rates or foreign currency exchange rates; and

- the impact of changes to tax legislation and, generally, our tax position.

This prospectus contains, and other statements that we may make may contain, forward-looking statements with respect to future financial or business performance, strategies or expectations. Forward-looking statements are typically identified by words or phrases such as "trend," "opportunity," "pipeline," "believe," "comfortable," "expect," "anticipate," "current," "intention," "estimate," "position," "assume," "potential," "outlook," "continue," "remain," "maintain," "sustain," "seek," "achieve" and similar expressions, or future or conditional verbs such as "will," "would," "should," "could," "may" or similar expressions.

Forward-looking statements are subject to numerous assumptions, risks and uncertainties, which change over time. Forward-looking statements speak only as of the date they are made, and we assume no duty to and do not undertake to update forward-looking statements. These forward-looking statements do not meet the safe harbor for forward-looking statements pursuant to Section 27A of the Securities Act or Section 21E of the Securities Exchange Act. Actual results could differ materially from those anticipated in forward-looking statements and future results could differ materially from historical performance.

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USE OF PROCEEDS

Unless otherwise specified in a prospectus supplement, we intend to use the net proceeds from any offering to repay amounts outstanding under the Revolving Facilities, if any, (which will increase the funds under the Revolving Facilities available to us to make additional investments in portfolio companies) and to make investments in portfolio companies in accordance with our investment objective and for otheFONT FACE="ARIAL" SIZE="2">Weighted average common shares outstanding:

Basic						
	15,000,100	8,717,831	23,717,931	15,000,100	8,813,763	23,813,863
Diluted						
	22,989,403	777,088	23,766,491	23,096,460	892,751	23,989,211

See accompanying notes to unaudited pro forma statements of income

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Notes to Unaudited Pro Forma Statements of Income

(1) Reflects the following adjustments:

(a) Elimination of $0.627 million and $0.479 million for the year ended December 31, 2006 and nine months ended September 30, 2007, respectively for the interest expense associated with the borrowings under both the term-loan portion of our senior secured loan agreement and the revolving credit facility.

(b) Elimination of the stock compensation expense of $1.040 million for the year ended December 31, 2006 and $2.903 million for the nine months ended September 30, 2007 associated with the Variable Plan, which includes a guarantee by us.

(c) Increased stock compensation expense of $0.996 million for the year ended December 31, 2006 related to the acceleration of certain stock option agreements. Increased stock compensation expense of $0.129 million for the year ended December 31, 2006 and $0.097 million for the nine months ended September 30, 2007 for the triggering event for the Regional Manager Stock Unit Plan.

(d) Increased stock compensation expense of $0.239 million for the year ended December 31, 2006 and $0.179 million for the nine months ended September 30, 2007 related to restricted stock grants of approximately 90,200 shares of common stock that we intend to grant to certain employees, whose salaries, commissions and benefits are recorded within selling, general and administrative expenses, and service providers at the closing of the initial public offering (which remains subject to approval by our board of directors).

(e) Increased stock compensation expense of $0.222 million for the year ended December 31, 2006 and $0.167 million for the nine months ended September 30, 2007 related to stock option grants that we intend to grant certain executive officers, employees, whose salaries, commissions and benefits are recorded within selling, general and administrative expenses, and service providers on the day this offering is priced for sale to the public to purchase approximately 125,000 shares of common stock at the initial public offering price (which remains subject to approval by our board of directors).

(f) Application of the appropriate statutory tax rates of the respective tax jurisdictions to which adjustments relate, 38.8% in 2006 and 38.5% in nine months ended September 30, 2007.

(g) Elimination of $0.051 million for the year ended December 31, 2006 and $0.039 million for the nine months ended September 30, 2007 associated with the accretion of redeemable preferred stock.

A $1 change, up or down, in the midpoint of the range shown on the cover page of this prospectus would change the stock compensation liability expense associated with the Variable Plan by $0.9 million.

(2) Pro forma basic and diluted net income per common share are computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period and include the effect of issuing additional shares of common stock at a price of $13.00 per share in this offering used to repay amounts outstanding under the term-loan portion and the revolving facility portion of our senior unsecured loan agreement.

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

	Year Ended December 31, 2006	Nine Months Ended September 30, 2007
Pro forma weighted average common shares outstanding, including preferred stock conversion to common stock	22,952,118	22,952,118
Effect of shares issued(3)	765,813	861,745
Pro forma weighted average common shares outstanding including effect of shares issued	23,717,931	23,813,863
Dilutive effect of stock options	48,560	175,348
Pro forma weighted average common shares and dilutive securities outstanding	23,766,491	23,989,211

(3) The effect of shares issued considers only those shares whose proceeds are being reflected in pro forma adjustments to the income statement rather than the full number of shares issued by us in this offering. The shares were determined as the quotient of our average debt balance over the period reflected in the pro forma income statement and the midpoint of the range shown on the cover page of this prospectus.

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SELECTED FINANCIAL DATA

You should read the data set forth below in conjunction with our financial statements and related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations, Unaudited Pro Forma Financial Information and other financial information included elsewhere in this prospectus. We derived the selected financial data as of December 31, 2005 and 2006 and for each of the years ended December 31, 2004, 2005 and 2006 from our audited financial statements and the related notes appearing elsewhere in this prospectus. We derived the selected financial data as of December 31, 2004 from our audited financial statements and the related notes not included in this prospectus. We derived the selected financial data as of and for the years ended December 31, 2002 and 2003 from our unaudited financial statements not included in this prospectus. The selected statements of income data for the nine months ended September 30, 2006 and 2007 and the selected balance sheet data as of September 30, 2007 have been derived from our unaudited financial statements appearing elsewhere in this prospectus which, in the opinion of our management, have been prepared on the same basis as the audited financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of our operating results and financial position for those periods and as of those dates. The selected unaudited financial data for the nine months ended September 30, 2007 are not necessarily indicative of our results for the year ending December 31, 2007 and our historical results are not necessarily indicative of our results for any future period.

	Year Ended December 31,					Nine Months Ended September 30,	
	2002	2003	2004	2005	2006(1)	2006(1)	2007(1)
	(in thousands, except share and per share amounts)						
	(unaudited)	(unaudited)				(unaudited)	(unaudited)
Statement of Income Data							
Net sales	$ 65,382	$ 100,866	$ 171,766	$ 244,947	$ 332,060	$ 247,219	$ 299,797
Cost of sales	43,051	67,870	115,857	158,844	221,931	163,955	200,404
Gross profit	22,331	32,996	55,909	86,103	110,129	83,264	99,393
Selling, general and administrative expenses	17,545	29,566	48,461	67,900	88,716	64,611	85,491
Impairment loss on long-lived assets		955	293				
Operating income	4,786	2,475	7,155	18,203	21,413	18,653	13,902
Interest expense	160	218	429	638	722	548	607
Other (income) expense(2)	(318)	(428)	190	(96)	(368)	(303)	(168)
Income before income taxes	4,944	2,685	6,536	17,661	21,059	18,408	13,463
Provision for income taxes(3)	163	65	(1,450)	6,948	8,161	7,133	5,185
Net income	$ 4,781	$ 2,620	$ 7,986	$ 10,713	$ 12,898	$ 11,275	$ 8,278
Net income per common share:							
Basic	$ 0.32	$ 0.17	$ 0.53	$ 0.71	$ 0.86	$ 0.75	$ 0.55
Diluted	$ 0.32	$ 0.17	$ 0.51	$ 0.46	$ 0.56	$ 0.49	$ 0.36
Weighted average common shares outstanding(4):							
Basic	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100	15,000,100

Diluted	15,000,100	15,000,100	15,675,477	23,063,174	22,989,403	23,001,681	23,096,460

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

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

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

	As of December 31,					As of September 30,
	2002	2003	2004	2005	2006	2007
			(in thousands)			
	(unaudited)	(unaudited)				(unaudited)
Balance Sheet Data						
Cash and cash equivalents	$ 384	$ 3,073	$ 3,031	$ 6,031	$ 3,965	$ 5,666
Merchandise inventories	9,501	14,910	22,507	30,009	51,758	74,944
Total assets	13,249	21,017	39,753	55,162	78,020	106,395
Total debt and capital lease obligations, including current maturities	2,555	2,617	12,364	10,360	9,603	14,275
Stock compensation liability	850	2,020	4,958	8,092	9,132	12,034
Redeemable preferred stock			34,693	34,744	34,795	34,834
Total stockholder s equity (deficit)	4,260	3,620	(30,242)	(18,775)	(5,468)	4,108
Working capital(1)	4,299	5,230	8,091	17,059	29,697	24,686

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

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MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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

Overview

Lumber Liquidators is the largest specialty retailer of hardwood flooring in the United States, based on total sales. We offer an extensive selection of premium hardwood flooring products from more than 25 domestic and exotic wood species under multiple proprietary brands, together with a broad assortment of flooring enhancements and installation accessories, at everyday low prices that appeal to a diverse customer base. We purchase flooring directly from supplier mills and brokers, thereby avoiding mark-ups by distributors. As of September 30, 2007, we sold our products through 111 Lumber Liquidators stores in 42 states, a call center, our website and a catalog. Our low-cost store model utilizes a no frills showroom with limited in-store inventory. We currently finish approximately 70% of our premium Bellawood products at our Toano finishing line and distribution center to ensure product quality and to reduce third-party finishing costs. Approximately 85% of our merchandise passes through this facility before we move it to our stores. We believe that our vertically integrated business model enables us to offer a broad assortment of high-quality products to our customers at a lower cost than our competitors.

The growth in our net sales has been driven by new store openings and our strong comparable store sales performance. In the period from January 1, 2003 to September 30, 2007, we opened 86 stores, representing more than three-quarters of our total store base. Our gross profit is driven primarily by the cost of acquiring the products we sell from our suppliers, but also includes inbound transportation costs from those suppliers to our distribution center or stores, customs and duty charges, transportation charges from our distribution center to our stores and the cost of delivering product purchases to the customer. Our most significant operating expenses have historically been our advertising expenses and our labor costs. Our advertising costs have generally declined as a percentage of net sales as we have expanded, but may vary from quarter to quarter with shifts in marketing strategy and the timing of our marketing campaigns. Our labor costs have also declined as a percentage of net sales, while increasing in absolute terms as a result of our investment in the store support infrastructure, including enhancements to our management team. We expect that our aggregate operating expenses will decline as a percentage of our net sales as we implement our growth strategy and our business continues to grow.

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

Investing in our infrastructure. In response to the rapid growth in the number of new store locations that began in 2003, we slowed the pace of new store openings in 2006 to focus on expanding our store support infrastructure. As part of this process, we have assembled an experienced executive team to manage our day-to-day operations and reinforce the foundation that will enable us to achieve our long-term growth objectives. In September 2006, we hired our chief executive officer, and our founder transitioned to become the chairman of our board of directors, where he remains actively involved in developing and executing our marketing strategy, and enhancing the relationships with our supplier mills and brokers. During 2006 and 2007, we also hired a number of individuals with significant experience in the specialty retail industry, including a new chief information officer, a senior vice president of store operations, a senior vice president of direct marketing and advertising, and a senior vice president of merchandising. We have also expanded our management structure by adding a senior vice president of supply chain and general corporate counsel. We have also restructured our regional operations by increasing the number of regional managers from eight to 15 to support future growth and assist in maintaining pricing and cost discipline.

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

Although the hardwood flooring market is projected to experience long-term growth, estimated at a compound annual growth rate of 7.4% through 2011, Catalina Research estimates that U.S. hardwood flooring square-foot sales declined 10.6% in 2006 and declined 14.1% in the first half of 2007 compared to the same period in 2006. Similar declines were estimated across most types of flooring, and were due in particular to decreased new housing demand. Despite these market declines, however, our net sales increased 36% in 2006 and 20% in the first six months of 2007. See Business Our Market. Although the majority of our sales are to consumers engaged in remodeling projects, a decline in new housing demand could cause a decline in remodeling or remodeling activity could decline for other reasons. See Risk Factors Risks Relating to Our Business and Industry The hardwood flooring industry depends on the economy, home remodeling activity, the homebuilding industry and other important factors. We believe that we will continue to benefit from several key long-term industry trends and characteristics, including increased home improvement spending resulting from aging housing stock, increasing home ownership, increasing average home size and favorable demographic trends as well as the expansion and evolution of the hardwood flooring market and the greater perceived attractiveness of hardwood flooring among consumers.

Assessing the Performance of Our Business

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

Net Sales

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

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Growth In Our Store Base. We opened 17 stores in 2004, 19 stores in 2005 and 16 stores in 2006, which contributed substantially to the growth of our net sales in those years. In 2006, we slowed the increase in new store locations as we expanded our store support infrastructure to better facilitate sustainable growth of both our net sales and gross margin. As of September 30, 2007, we had opened 20 new stores and had signed leases for seven additional stores. We plan to open at least 25 new stores in total during 2007 and between 30 and 40 new stores during each of the next several years thereafter. The cost required to open a typical new store is approximately $240,000, of which inventory, net of trade payables, represents approximately $190,000. Our new stores have historically opened with an initial ramp-up period typically lasting from 36 to 48 months or more, during which they generated sales below the levels at which we expect them to normalize. Our average new store across our markets has, however, historically become profitable within three months of beginning operations and returned its initial cash investment within seven months. See Risk Factors Risks Related to Our Business and Industry The planned rapid increase in the number of our stores may make our future results unpredictable.

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

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

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

Gross Profit and Gross Margin

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

our sales volumes and the margins on products we sell;

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

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

customs and duty charges on international purchases;

the cost of third-party carrier services providing customer deliveries;

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

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

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

Selling, General, Administrative and Other Operating Expenses

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

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

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

Other Factors Affecting Our Results

Equity Compensation Expenses

We maintain four equity compensation plans: a newly adopted equity compensation plan for employees, non-employee directors and other service providers (the 2007 Plan); a stock option plan for executive management; a stock option plan for non-employee members of our board of directors; and a stock unit plan for regional store management. The 2007 Plan was adopted in August 2007, and we have not issued any stock options or stock-based awards under that plan. No further awards will be granted under the prior stock option plans following this offering. We have not recorded any compensation expense relating to the stock unit plan because those units would have expired without value unless an IPO or sale event occurs before 2011. In addition, we intend to make restricted stock grants to certain employees and service providers and stock option grants to certain executive officers, employees and service providers at the closing of the initial public offering. In connection with this offering, we expect to incur a charge of approximately $1.2 million (based on the midpoint of the range shown on the cover page of this prospectus) in the quarter of 2007 in which this transaction closes relating to the stock unit plan and acceleration of options under the 2004 and 2006 stock option plans.

We are also party to the Variable Plan, an agreement between Tom Sullivan and Kevin Sullivan, Tom s brother, who started our western U.S. operations and was our first regional manager, pursuant to which we generally guarantee Tom s cash payment obligation under the agreement. We account for that agreement as a variable performance plan. Under the Variable Plan, as amended in August 2005, Kevin has the right to a fixed ownership percentage of Lumber Liquidators, Inc. on a fully diluted basis, plus an additional ownership percentage based on certain performance criteria. This right is exercisable for shares of common stock, to be contributed by Tom and which have been placed in escrow, in conjunction with an IPO or sales event. Kevin s right under the plan will be considered to be exercised in full immediately prior to the completion of the initial public offering and, accordingly, we do not expect to record any future charges relating to the Variable Plan other than an adjustment in the quarter in which this transaction closes to reflect the difference between the midpoint of the range shown on the cover page of this prospectus and the final closing price for the number of shares considered earned by Kevin. Before the Variable Plan was amended in August 2005, we recorded stock-based compensation expense based on Kevin having earned a 5% ownership interest on a fully diluted basis (in conformity with the terms of that agreement). We recorded stock-based compensation expense relating to the Variable Plan of $2.9 million in the first nine months of 2007, $1.0 million in 2006, $3.1 million in 2005 and $2.9 million in 2004, and carried a short-term liability on our balance sheet relating to the agreement of $12.0 million at September 30, 2007. See Risk Factors Risks Relating to Our Business and Industry We will incur non-cash compensation expenses, and may be required to issue shares of common stock, in connection with existing stock-based compensation agreements. A $1 change, up or down, between the price set forth above and the price of stock on the trading day before the closing of this offering would change the non-cash compensation expense associated with the Variable Plan by $0.9 million.

In addition, we had an employment agreement and a stock warrant plan with a former senior executive (who resigned on May 31, 2006). The former executive has filed a demand for arbitration alleging that he terminated his employment for good reason, as defined in his employment agreement and the warrant plan. In his demand for arbitration, the former senior executive contends that we

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breached our obligations to him upon his resignation of employment. He is seeking damages of approximately $0.7 million (plus the value of certain other specified benefits), as well as a declaration that he has owned 1% of the company since he terminated his employment. An arbitration hearing was held on October 1-2, 2007. The parties will be afforded the opportunity to submit post-arbitration briefs and additional testimony and evidence may be presented. Stock-based compensation expenses under this plan for 2005 and 2004 were reversed in 2006 upon separation, with an offset to additional capital. See Business Legal Proceedings.

For additional information regarding our equity compensation plans, see Management Executive Compensation and Note 7 to our audited financial statements and Note 4 to our unaudited condensed financial statements.

Income Taxes

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

Results of Operations

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

	Year Ended December 31,			Nine Months Ended September 30,		Three Months Ended September 30,	
	2004	2005	2006	2006	2007	2006	2007
	(in millions, except percentages and numbers of stores)						
Net sales	$ 171.8	$ 244.9	$ 332.1	$ 247.2	$ 299.8	$ 83.1	$ 102.1
Comparable store sales increase from prior year	*38.2%*	*19.0%*	*17.3%*	*19.2%*	*8.6%*	*12.8%*	*8.4%*
Number of stores opened in period(1)	*17*	*19*	*16*	*9*	*20*	*1*	*8*
Cost of sales	115.9	158.8	221.9	164.0	200.4	55.7	67.6
Gross profit	55.9	86.1	110.1	83.3	99.4	27.4	34.4
SG&A expenses	48.5	67.9	88.7	64.6	85.5	22.6	28.3
Operating income	7.2	18.2	21.4	18.7	13.9	4.8	6.2
Net income(2)	8.0	10.7	12.9	11.3	8.3	2.9	3.7

	Year Ended December 31,			Nine Months Ended September 30,		Three Months Ended September 30,	
	2004	2005	2006	2006	2007	2006	2007
	(% of net sales)						
Net sales	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of sales	67.5%	64.8%	66.8%	66.3%	66.8%	67.0%	66.2%
Gross profit	32.5%	35.2%	33.2%	33.7%	33.2%	33.0%	33.8%
SG&A expenses	28.2%	27.7%	26.7%	26.1%	28.5%	27.2%	27.7%
Operating income	4.2%	7.4%	6.4%	7.5%	4.6%	5.8%	6.1%
Net income(2)	4.6%	4.4%	3.9%	4.6%	2.8%	3.5%	3.6%

(1) In May 2006, we closed a laminate flooring-only store that had been established to operate during the remaining lease period of a relocated store.

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

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Three Months Ended September 30, 2007 Compared to Three Months September 30, 2006

Net Sales. Net sales increased approximately $19.0 million, or 23%, to $102.0 million for the three months ended September 30, 2007 from $83.1 million for the three months ended September 30, 2006. This increase was primarily driven by an increase of $11.9 million in non-comparable store sales, including $6.0 million at the 20 stores opened in 2007, and by an increase of $7.1 million, or 8.4%, in comparable store sales. Increases in comparable store sales were driven primarily by the continued maturation of stores in operation for 13 to 36 months, where net sales increased $5.3 million, or 25%, and by generally strong consumer demand for our expanded product assortment, including new lines of hand-scraped solid and engineered hardwoods, more durable laminates and strand bamboo, introduced late in the second quarter of 2007. Net sales benefited from an increase in sales volume, primarily measured in square footage, and an increase in the average retail price per unit sold. In addition, moldings and accessories, generally add-on purchases, increased $2.6 million, or 36%, and represented 10% of total sales in the three months ended September 30, 2007.

Gross Profit and Gross Margin. Gross profit increased approximately $7.0 million, or 26%, to $34.4 million for the three months ended September 30, 2007 from $27.4 million for the three months ended September 30, 2006, principally due to increases in net sales partially offset by a net higher cost from suppliers for the merchandise sold and an overall increase in transportation costs. Gross margin for the three months ended September 30, 2007 increased approximately 80 basis points to 33.8% from 33.0% for the three months ended September 30, 2006. This increase was primarily a result of the sales strength of new product lines introduced late in the second quarter of 2007, including new lines of hand-scraped solid and engineered hardwoods, more durable laminates and strand bamboo. These products typically carry a higher average retail price per unit and a higher gross margin than our average product, and are a part of the initiative we began in 2006 to broaden our assortment and the price points available to our customers. Logistics initiatives implemented in the three month period ended September 30, 2007 benefited gross margin through reductions in both the number of miles driven by trucks supplying our products and the per-mile cost of transporting our products. This benefit was partially offset by greater per unit international transportation costs, including the implementation or increase of a number of key tariffs assessed on imported products, most notably bamboo and certain products from Brazil.

Operating Income. Operating income for the three months ended September 30, 2007 increased $1.4 million, or 29%, to $6.2 million, as the $7.0 million increase in gross profit was partially offset by a $5.7 increase in SG&A expenses, principally due to the following factors:

Salaries, commissions and benefits increased $2.7 million, or 37%, primarily due to the increase in the number of new store locations and the significant investment in executive and operational management within our store support infrastructure. The investment in executive and operational store support management during 2006 included our new chief executive officer in September 2006 and the addition of six regional managers and two senior executive positions that did not exist at September 30, 2006. In addition, we added more finance, compliance and information technology control personnel in 2007 as we prepared to become a public company. Accordingly, as a percentage of net sales, salaries, commissions and benefits increased to 10.0% for the three months ended September 30, 2007 from 9.0% for the same period in 2006.

Advertising expenses increased $1.3 million, or 14%, primarily due to the expansion of both our national advertising branding campaign through television, radio and sports marketing, and our direct mail programs. As a percentage of net sales, however, advertising expenses decreased to 10.2% for the three months ended September 30, 2007 from 11.0% for the same period in 2006 as we were able to leverage the expansion of our national advertising campaign over increased sales.

Occupancy costs increased $0.8 million, or 30%, and also increased to 3.3% from 3.1% as a percentage of net sales, as the increase in costs related to new stores openings, including 18 opened in the second and third quarter, were only partially offset by increases in net sales. Six new stores were opened in the second and third quarters of 2006.

Depreciation and amortization increased $0.2 million, but remained a constant 0.9% as a percentage of net sales.

Stock-based compensation expense decreased $0.2 million. A reduction in the compensation associated with the Variable Plan was partially offset by increased stock-based compensation expense related to stock options granted after September 30, 2006.

Certain other expenses, including legal and professional fees, increased approximately $0.8 million, primarily as we prepared to become a public company. Further, certain banking fees, including bankcard discounts, increased commensurate with sales.

As a percentage of net sales, operating income increased to 6.1% for the three months ended September 30, 2007 from 5.8% for the three months ended September 30, 2006. This increase was primarily due to the increase in gross margin to 33.8% and SG&A expenses to 27.7% for the three months ended September 30, 2007 from 33.0% and 27.2%, respectively, for the three months ended September 30, 2006.

Net Income. Net income increased approximately $0.8 million to $3.7 million for the three months ended September 30, 2007 from $2.9 million for the three months ended September 30, 2006 and increased as a percentage of net sales to 3.6% for the three months ended September 30, 2007 from 3.5% for the three months ended September 30, 2006. Our effective income tax rate was approximately 38.3% for the three months ended September 30, 2007 and 38.7% for the three months ended September 30, 2006, reflecting slight variances in state income tax rates.

Nine Months Ended September 30, 2007 Compared to Nine Months Ended September 30, 2006

Net Sales. Net sales increased approximately $52.6 million, or 21%, to $299.8 million for the nine months ended September 30, 2007 from $247.2 million for the nine months ended September 30, 2006. This increase was primarily driven by an increase of $31.3 million in non-comparable store sales, including $8.6 million at the 20 stores opened in 2007, and an increase of $21.3 million, or 8.6%, in comparable store sales. Increases in comparable store sales were driven primarily by the continued maturation of stores in operation for 13 to 36 months, where net sales increased $14.9 million, or 26.1%, and generally strong consumer demand for our expanded product assortment. Net sales benefited from an increase in sales volume, primarily measured in square footage, and an increase in the average retail price per unit sold. Increased demand was driven in part by strength in the sales of the Bellawood line, particularly exotic hardwoods, and the broader assortment of engineered hardwoods, including an expanded offering of hand-scraped products, which offset declines in sales of liquidation deals and unfinished hardwoods. Further, for the nine month period ended September 30, 2007, moldings and accessories increased $8.9 million, or 46%, and represented 10% of total sales in the nine months ended September 30, 2007, up from 8% of total sales for the same period in 2006.

Gross Profit and Gross Margin. Gross profit increased approximately $16.1 million, or 19%, to $99.4 million for the nine months ended September 30, 2007 from $83.3 million in first nine months of 2006, principally due to increases in net sales partially offset by a net higher cost from suppliers for the merchandise sold and an increase in transportation costs. Gross margin for the nine months ended September 30, 2007 decreased approximately 50 basis points to 33.2% from 33.7% for the nine months ended September 30, 2006. This decrease resulted principally from our efforts to broaden our product assortment and the range of retail price points available to our customers, an initiative we began in the first quarter of 2006. We initially introduced prefinished engineered hardwood lines, which drove

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increases in net sales and gross profit, but those products typically carry a margin lower than our average product. Late in the second quarter of 2007, we introduced new hand-scraped solid and engineered hardwoods, more durable laminates and strand bamboo lines that have a higher than average gross margin. Increases in domestic and international transportation costs also caused gross margin to decline, as per-mile ground charges increased primarily due to higher fuel costs, and the implementation or increase in 2007 of a number of key tariffs assessed on imported products, most notably bamboo. These increases were partially offset by decreases in our transportation costs resulting from logistic initiatives, implemented in the third quarter of 2007, that are designed to reduce both the miles driven by trucks supplying our stores and the per mile cost of shipping our products.

Operating Income. Operating income for the nine months ended September 30, 2007 decreased $4.8 million, or 26%, to $13.9 million, as a $20.9 million increase in SG&A expenses was partially offset by a $16.1 million increase in gross profit, principally due to the following factors:

- Salaries, commissions and benefits increased $7.8 million, or 37%, primarily due to the increase in the number of new store locations and the significant investment in executive and operational management within our store support infrastructure. The investment in executive and operational store support management during 2006 included our new chief executive officer, four senior executive positions supporting the stores and six regional store managers. In addition, we added more finance, compliance and information technology control personnel in 2007 as we prepared to become a public company. Accordingly, as a percentage of net sales, salaries, commissions and benefits increased to 9.7% for the nine months ended September 30, 2007 from 8.6% for the nine months ended September 30, 2006.

- Advertising expenses increased $4.9 million, or 18%, for the nine months ended September 30, 2007, primarily due to the expansion of our national advertising branding campaign through television, radio and sports marketing, coupled with local advertising and direct mail programs. As a percentage of net sales, however, advertising expenses decreased to 10.6% for the nine months ended September 30, 2007 from 10.9% for the comparable period in 2006, as we were able to leverage that expansion over larger increases in net sales.

- Stock-based compensation expense increased $3.4 million to $4.2 million for the nine months ended September 30, 2007 from $0.8 million in the first nine months of 2006, primarily due to an increase of $2.1 million in the stock compensation calculated under the Variable Plan and $1.0 million in stock compensation expense related to stock options granted in July and October 2006 and April 2007.

- Occupancy costs increased $1.6 million, but remained a consistent 3.0% as a percentage of net sales, as costs related to the opening of 26 store locations since September 30, 2006 were offset by increases in net sales.

- Depreciation and amortization increased $0.5 million but remained a constant 0.9% as a percentage of net sales.

- Certain other expenses, including legal and professional fees, increased $2.7 million as we enhanced our financial reporting, legal and regulatory compliance, internal controls and corporate governance. Further, certain banking fees, including bankcard discounts, increased commensurate with sales.

As a percentage of net sales, operating income declined to 4.6% for the nine months ended September 30, 2007 from 7.5% for the nine months ended September 30, 2006. This decrease was primarily due to the decline in gross margin and an increase in SG&A expenses as a percentage of net sales to 28.5% for the nine months ended September 30, 2007 from 26.1% for the nine months ended September 30, 2006.

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Net Income. Net income decreased approximately $3.0 million to $8.3 million for the nine months ended September 30, 2007 from $11.3 million for the nine months ended September 30, 2006 and declined as a percentage of net sales to 2.8% for the nine months ended September 30, 2007 from 4.6% for the nine months ended September 30, 2006. Our effective income tax rate was approximately 38.5% for the nine months ended September 30, 2007 and 38.7% for the nine months ended September 30, 2006, reflecting slight variances in state income tax rates.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Stock-based compensation expense decreased due to lower current-year expense associated with the Variable Plan, which was partially offset by expense related to stock options granted in 2006.

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

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

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

Net Sales. Net sales increased $73.2 million, or 43%, to $244.9 million in 2005 from $171.8 million in 2004. This increase was primarily driven by an increase of $32.6 million, or 19.0%, in comparable store sales, and also by additional non-comparable store sales of $18.3 million at the 17 stores opened during 2004 and $22.2 million at the 19 new stores opened during 2005. Comparable store sales increases were driven principally by maturation of new stores, expansion of our product mix

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and increased traffic across our store base. The average retail price per unit sold also increased slightly. Overall net sales increased due principally to the following factors:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Quarterly Results and Seasonality

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

	2005 Quarter Ended (unaudited)					2006 Quarter Ended (unaudited)(1)(2)					2007 Quarter Ended (unaudited)(1)(2)		
	Mar. 31,	June 30,	Sept. 30,	Dec. 31,	Total	Mar. 31,	June 30,	Sept. 30,	Dec. 31,	Total	Mar. 31,	June 30	Sept. 30
	(in millions)					(in millions)					(in millions)		
Net sales	$ 50.8	$ 61.6	$ 63.2	$ 69.3	$ 244.9	$ 76.1	$ 88.1	$ 83.1	$ 84.8	$ 332.1	$ 92.0	$ 105.7	$ 102.1
Gross profit	18.0	21.2	22.4	24.5	86.1	26.4	29.5	27.4	26.8	110.1	30.6	34.4	34.4
Operating income	3.5	5.5	5.7	3.5	18.2	5.9	8.0	4.8	2.7	21.4	3.8	4.0	6.2
Net income	2.1	3.2	3.3	2.1	10.7	3.6	4.8	2.9	1.6	12.9	2.3	2.3	3.7

(1) Reflects expense relating to the Variable Plan in 2006 and 2007 of $0.26 million for the quarters ended March 31, June 30, September 30 and December 31, 2006 and $0.40 million, $2.65 million and $(0.15) million in the quarters ended March 31, June 30 and September 30, 2007.

(2) Reflects depreciation and amortization expense in 2006 and 2007 of $0.60 million, $0.76 million, $0.76 million and $0.79 million in the quarters ended March 31, June 30, September 30 and December 31, 2006 and $0.82 million, $0.85 million and $0.93 million in the quarters ended March 31, June 30 and September 30, 2007.

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

Our quarterly results of operations fluctuate depending on the timing of our advertising expenses and the timing of and income contributed by new stores. Our performance has also been impacted by

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certain of our initiatives to improve our infrastructure and to position our business to support sustainable growth and profitability in the future, including in particular the hiring of additional management personnel in the second half of 2006, as well as the steps we took to optimize inventory levels in the fourth quarter of 2006.

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

Liquidity and Capital Resources

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

Our principal sources of liquidity as of September 30, 2007 consisted of $5.7 million in cash and cash equivalents and $17.8 million of availability under our new $25.0 million revolving credit facility.

We will use proceeds from this offering to repay all amounts outstanding under the term-loan portion of our senior secured loan agreement and our new revolving credit agreement (approximately $14.1 million in aggregate as of September 30, 2007). We will use the remainder of the proceeds for general corporate purposes, including providing additional long-term capital to support the growth of our business (primarily through opening new stores) and maintaining our existing stores.

Cash and Cash Equivalents

During the first nine months of 2007, cash and cash equivalents increased $1.7 million to $5.7 million. Operating activities provided $3.4 million, and proceeds provided by borrowings were $6.4 million, partially offset by the use of $4.8 million to purchase property and equipment and $1.8 used to repay scheduled principal on long-term debt and capital leases. During the first nine months of 2006, cash and cash equivalents decreased $1.7 million to $4.4 million, as $0.9 million of cash provided by operating activities and $1.1 million in proceeds provided by borrowings were more than offset by $2.1 million used to purchase property and equipment, and $1.6 million used to repay scheduled principal on long-term debt and capital leases.

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

Cash Flows

Operating Activities. Net cash provided by operating activities was $3.4 million for the nine months ended September 30, 2007 and $0.9 million for the nine months ended September 30, 2006. This increase in net cash provided by operating activities resulted primarily from changes in working capital,

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particularly an increase in customer deposits and store credits, partially offset by a greater increase in inventory levels, a lower increase in accounts payable and a decrease in net income in the first nine months of 2007 compared to the first nine months of 2006.

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

Investing Activities. Net cash used in investing activities was $4.8 million for the nine months ended September 30, 2007 and $2.1 million for the nine months ended September 30, 2006. Net cash used in investing activities during 2007 primarily related to capital purchases of truck trailers that we use to move our merchandise from our warehouse to our stores, new store capital needs (primarily store fixtures and leasehold improvements), and information technology (IT) costs, including costs related to our new point of sale system and routine purchases of computer hardware and software. Net cash used in investing activities during the nine months ended September 30, 2006 primarily related to new store capital needs and an upgrade of our telephone system and website.

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

We expect that our capital expenditures for 2007 will be approximately $7.0 million, relating primarily to store fixtures and leasehold improvements for new stores, as well as additional trailers, upgrades to our finishing line and IT costs relating to our new point-of-sale system, maintenance and our website. We had opened 20 new store locations through September 30, 2007, and we intend to open at least 25 new stores in total during 2007 and between 30 and 40 new stores during each of the next several years thereafter. We believe that our cash flow from operations, together with our existing liquidity sources and the net proceeds from this offering, will be sufficient to fund our operations and anticipated capital expenditures over at least the next 24 months.

Financing Activities. Net cash provided by (used in) financing activities was $3.0 million for the nine months ended September 30, 2007 and ($0.5) million for the nine months ended September 30, 2006. Net cash provided by financing activities for both periods was attributable to borrowings under our revolving credit facility, offset by principal payments on our senior loan agreements and capital lease obligations. In the nine month period ended September 30, 2007, we used $1.6 million for the payment of IPO costs.

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

Senior Secured Loan Agreement

In March 2006, we entered into an amended and restated senior secured loan agreement with Bank of America, N.A. (Lender), which was amended in July 2006 to increase the size of the revolving credit facility. Under the agreement, we have a term loan with an original principal amount of $9.9 million and a revolving credit facility of up to $10.0 million. We are required to repay the principal amount under the term loan in 60 equal monthly installments with the first payment due on April 1, 2006 and the final payment due on March 1, 2011. The revolving credit facility was repaid in full in connection with our entry into a new revolving credit agreement in August 2007.

The term loan portion of the senior secured loan agreement bears interest on the outstanding balance at a per annum rate equal to the Base Rate (generally equal to one-month LIBOR (floating daily), subject to adjustments in certain circumstances) plus the Applicable Margin (as defined in the facility). The Applicable Margin depends on the Funded Debt to EBITDAR Ratio (as defined in the facility), and can range from 0.45% to 1.15% so long as the Base Rate is linked to one-month LIBOR (floating daily). As of December 31, 2006 and September 30, 2007, the Applicable Margin was 0.90%, and the rate at which we accrued interest was 6.2% and 6.0%, respectively. We are required to pay an unused commitment fee of 0.25% per annum on undrawn amounts under the revolving credit facility.

The senior secured loan agreement and related security agreement contain a number of restrictions that will require us to maintain certain financial ratios and limit our ability, among other things, to borrow money, pledge our inventory or other assets as security in other borrowings or transactions, undergo a merger or consolidation, guarantee certain obligations of third parties, make or extend credit other than on ordinary terms in the course of our business or engage in any activity not reasonably related to those we presently conduct.

We were in compliance with all of our covenants under the loan agreement as of December 31, 2006 and September 30, 2007. As of December 31, 2006, we had remaining obligations of $9.1 million, to repay amounts outstanding under the loan agreement. We refinanced amounts outstanding under the revolving facility portion of our senior secured loan agreement in August 2007 when we entered into our new revolving credit agreement. As of September 30, 2007, we had remaining obligations of $6.9 million under the term-loan portion of our senior secured loan agreement

Revolving Credit Agreement

In August 2007, we entered into a new revolving credit agreement to replace the revolving credit facility under the senior secured loan agreement. We can borrow up to $25.0 million under the new agreement, which expires on August 10, 2012.

Amounts outstanding under the new revolving credit agreement bear interest at a per annum rate equal to BBA LIBOR (equal to one-month LIBOR (reset on the 10th of the month), subject to adjustments in certain circumstances) plus the Applicable Margin (as defined in the revolving credit agreement). The Applicable Margin depends on the Funded Debt to EBITDA Ratio (as defined in the agreement), and can range from 0.50% to 1.00%. As of September 30, 2007, the Applicable Margin was 0.50%, and the rate at which we accrued interest was 6.3%. The agreement permits letters of credit to be drawn in an aggregate amount of $5.0 million and has no mandated payment provisions. We are required to pay an unused commitment fee of 0.125% per annum, which may be increased in the future based on financial performance criteria, on undrawn amounts under the agreement.

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The revolving credit agreement and related security agreement contain a number of restrictions that will require us to maintain certain financial ratios and limit our ability, among other things, to borrow money, pledge our inventory or other assets as security in other borrowings or transactions, undergo a merger or consolidation, guarantee certain obligations of third parties, make or extend credit other than on ordinary terms in the course of our business or engage in any activity not reasonably related to those we presently conduct.

We were in compliance with all of our covenants under our revolving credit agreement as of September 30, 2007 and, as of that date, had outstanding obligations of $7.2 million thereunder.

Issuance of Preferred Stock

In December 2004, funds managed by TA Associates purchased 7,952,018 shares of series A convertible preferred stock, par value $0.01, for $35.0 million. In connection with this sale, we declared a 150,000:1 common stock dividend to increase the number of common shares held by Tom from 100 to approximately 15.0 million. The stock split was effected in order to ensure that Tom would continue to hold an appropriate percentage of our common stock upon conversion of the convertible preferred stock held by TA Associates on a 1 for 1 basis. We distributed $42.6 million in cash to Tom in 2004, including $30.0 million of the proceeds from the sale of the convertible preferred stock (which represented a significant dilution of his ownership interest), $5.0 million to enable him to pay taxes on deemed income during the period we were an S corporation and $7.6 million of additional cash. We retained $5.0 million of cash from the sale of our Series A convertible preferred stock for general working capital purposes and to provide operating liquidity. As a result of those cash distributions, we had a total stockholder s deficit of $30.2 million as of December 31, 2004, which has steadily improved to stockholder s equity of $4.1 million as of September 30, 2007. In connection with this offering, TA Associates has agreed to convert all of the outstanding shares of series A convertible preferred stock that it holds into shares of common stock. For additional information about the investment by TA Associates, see Certain Relationships and Related Party Transactions Investment by TA Associates.

Related Party Transactions

Tom Sullivan is the sole owner of ANO LLC, DORA Real Estate Company, LLC and Wood on Wood Road, Inc., and he has a 50% membership interest in BMT Holdings, LLC (collectively, ANO and Related Companies). We leased our Toano facility, which includes a store location, and 25, 22 and 12 of our other store locations from these entities as of December 31, 2006, 2005 and 2004, representing 28.6%, 30.3% and 22.8% of total store leases, respectively. As of September 30, 2007, we leased our Toano facility and 26 of our other store locations from these entities, representing 24% of total store leases. The operating lease for our Toano facility has a base period through December 31, 2019. See Certain Relationships and Related Party Transactions.

Contractual Commitments and Contingencies

Our significant contractual obligations and commitments as of December 31, 2006 and September 30, 2007 are summarized in the following tables:

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

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	Total	Less Than 1 Year	1 to 3 Years	3 to 5 Years	5+ Years
	Payments Due by Period (in thousands)				
Contractual obligations(1)					
As of September 30, 2007					
Debt obligations	$ 14,165	$ 9,225	$ 3,952	$ 988	$
Variable rate interest on debt obligations(5)	781	376	374	31	
Operating lease obligations(3)	42,290	7,454	12,636	8,134	14,066
Capital lease obligations, including interest(3)	110	103	7		
Supplier purchase commitments(4)	47,959	25,376	22,583		
Total contractual obligations	$ 105,305	$ 42,534	$ 39,552	$ 9,153	$ 14,066

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

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

(3) Included in this table is the base period or current renewal period for our operating leases. We lease certain buildings and equipment under non-cancelable operating leases and certain transportation equipment under non-cancelable capital leases. The leases expire at various dates through 2017 (2019 in the case of the lease for our Toano facility). The operating leases generally contain renewal provisions for varying periods of time.

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

(5) As of September 30, 2007, our senior secured loan agreement accrued interest at a rate of one-month LIBOR plus 0.90%, and the rate at which we accrued interest was 6.0%. We estimated our obligation under this agreement by assuming that interest will accrue at the September 30, 2007 rate until the loan agreement expires.

Off-Balance Sheet Arrangements

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

Qualitative and Quantitative Disclosures About Market Risk

Interest Rates. Because our senior secured loan agreement and our new revolving credit agreement bear interest at a variable rate, we are exposed to market risks relating to changes in interest rates. Both agreements, which we expect to repay in full upon completion of this offering, bear interest at a variable rate, adjusted annually, based on our performance under certain specified operating ratios. From inception at March 23, 2006 to August 10, 2007, our outstanding loans bore interest at a per annum rate equal to one-month LIBOR plus 0.90%. From August 10 to September 30, 2007 the senior secured loan agreement and our new revolving credit facility bore interest at a per annum rate equal to one-month LIBOR plus 0.90% and 0.50%, respectively. A hypothetical 100 basis-point increase from the current interest level on $14.1 million, the aggregate amount outstanding under the term loan portion of our senior secured loan agreement and our new revolving credit facility at September 30, 2007, would result in approximately a $0.1 million increase in interest expense over a one-year period. A hypothetical 100 basis-point decrease from the current interest level would result in approximately a $0.1 million decrease in interest expense over a one-year period. We currently do not engage in any interest rate hedging activity and currently have no intention to do so in the foreseeable future. However, in the future, in an effort to mitigate losses associated with these risks, we may at times enter into derivative financial instruments, although we have not historically done so. We do not, and do not intend to, engage in the practice of trading derivative securities for profit.

Inflation

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

Critical Accounting Policies and Estimates

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

Recognition of Net Sales

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

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Equity Compensation

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

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

- Expected life of 7.5 years;
- Expected stock price volatility of between 35% and 39%, based on the median volatility of companies in a peer group;
- Risk-free interest rates from 4.6% to 5.2%; and
- Dividends are not expected to be paid in any year.

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

Management estimated the fair value of our common stock based on contemporaneous valuations utilizing a market-approach model. We used this approach to value our common stock in retrospectively determining stock-based compensation expense as of December 31, 2003, 2004 and 2005, and to establish contemporaneous fair values of equity instruments for our equity grants in 2006 and April 2007. For the second and third quarters of 2007, however, management determined that the IPO process had progressed to such an extent that a different valuation methodology (based on estimating the company s fair value as a public entity, and then applying a marketability discount) could be used to measure fair value, and accordingly used that methodology in determining stock compensation expense. We will make valuation determinations for the option grants and restricted stock unit grants that we intend to make (subject to approval by our board of directors) in connection with the IPO using the actual IPO price, and thereafter expect to use the market value of the common stock on any date on which any such determination is required to be made.

A variety of qualitative and quantitative factors were considered in making these equity valuation determinations, including the state of the economy and the industry in which we operate, milestones that the company and its management had achieved and the appropriate marketability discount. We discuss our market and our achievements to date elsewhere in this prospectus, including in the sections entitled Management s Discussion and Analysis of Financial Condition and Results of Operations and Business . A marketability discount was also applied in each case, which management determined to be reasonable for each period based on the company s prospects for liquidity at that time and developments in its business and operations. This discount decreased over time as we improved various aspects of our

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business and operations, including moving to a new facility, increasing the size of our product range, opening a significant number of new stores, hiring a number of key senior executives (including a new CEO), and implementing a number of operational, financial and governance policies to enhance our reporting and compliance functions.

We have not granted any stock options since April 2007. As of September 30, 2007, there were 1,846,847 stock options outstanding (including 50,000 stock options granted in April 2007), with an aggregate intrinsic value of $9.7 million. Of these, 261,260 stock options with an intrinsic value of $1.4 million were exercisable at September 30, 2007. See Note 4 to our unaudited condensed financial statements included elsewhere in this prospectus. Based on the midpoint of the estimated IPO price range, the intrinsic value of the stock options outstanding at September 30, 2007 would have been $9.7 million.

Merchandise Inventories

We value our merchandise inventories at the lower of merchandise cost or market value. We determine merchandise cost using the average cost method. All of the hardwood flooring we purchase from suppliers is either prefinished or unfinished, but is in immediate saleable form. To the extent that we finish and box unfinished products, we include those costs in the average unit cost of related merchandise inventory. In determining market value, we make judgments and estimates as to the market value of our products, based on factors such as historical results and current sales trends. Any reasonably likely changes that may occur in those assumptions in the future may require us to record charges for losses or obsolescence against these assets, but would not be expected to have a material impact on our financial condition or operating performance.

New Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109.* FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109. FIN 48 describes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective as of January 1, 2007. The adoption of FIN 48 did not have a material effect on our financial position or results of operations.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption is permitted. We are currently evaluating the impact of SFAS 157 on our financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits entities to choose, at specified election dates, to measure eligible items at fair value (fair value option) and to report in earnings unrealized gains and losses on those items for which the fair value has been elected. SFAS 159 also requires entities to display the fair value of those assets and liabilities on the face of the balance sheet. SFAS 159 establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 will be effective for us as of the first quarter of 2008. Early adoption is permitted. We are currently evaluating the impact of SFAS 159 on our financial statements.

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BUSINESS

Overview

Lumber Liquidators is the largest specialty retailer of hardwood flooring in the United States, measured by total sales and based on information from *Floor Covering Weekly* and *Floor Focus* and our industry experience. We believe we have achieved a reputation for offering great value, superior service and a broad selection of high-quality hardwood flooring products. We offer an extensive selection of premium hardwood flooring products under multiple proprietary brands at everyday low prices designed to appeal to a diverse customer base. We believe that our vertically integrated business model enables us to offer a broad assortment of high-quality products to our customers at a lower cost than our competitors. We purchase prefinished and unfinished flooring directly from mills or associated brokers and work with our suppliers to control costs, develop new products and ensure superior product quality. Approximately 80% of our sales are to existing homeowners engaged in remodeling projects, and the remainder are to small independent contractors engaged in remodeling and new home building projects. As of September 30, 2007, we sold our products through 111 Lumber Liquidators stores in 42 states, a call center, our website and a catalog. We believe that our brands, value proposition and integrated multi-channel approach are important competitive advantages.

We offer hardwood flooring products from more than 25 domestic and exotic wood species in both prefinished and unfinished brands of various widths and lengths. Our products are differentiated in terms of quality and price based on the species, grade of the hardwood, quality of finishing, as well as the length of the warranty. We also offer a broad assortment of flooring enhancements and installation accessories including moldings, noise-reducing underlays and adhesives. Our product offering is substantially comprised of our proprietary brands, including our premium Bellawood brand as well as our Builder s Pride, Virginia Mill Works, Schôn, Morning Star Bamboo and Dream Home brands. We have experienced strong historical growth, including net sales growth from $171.8 million in 2004 to $332.1 million in 2006, operating income growth from $7.2 million in 2004 to $21.4 million in 2006 and net income growth from $8.0 million in 2004 to $12.9 million in 2006, representing compound annual growth rates of approximately 39%, 73% and 27%, respectively. In the first nine months of 2007, our net sales were $299.8 million, which represents a 21% increase over the first nine months of 2006. Our operating income for the first nine months of 2007 declined to $13.9 million from $18.7 million in the first nine months of 2006, and our net income declined to $8.3 million from $11.3 million for the same periods. Our overall growth has been driven in large part by the opening of 86 stores since January 1, 2003 and our strong comparable store sales performance in each of those periods. On an annual basis, comparable store sales increased 19.0% from 2004 to 2005, and 17.3% from 2005 to 2006. In the first nine months of 2007, comparable store sales increased 8.6% over the first nine months of 2006, which increased 19.2% over the first nine months of 2005.

Our company started in 1994 when Tom Sullivan, the chairman of our board of directors, began selling discounted building materials. In 1996, he identified an opportunity to sell hardwood flooring at liquidator prices. Tom started selling unsold flooring products sourced directly from mills from a warehouse in Stoughton, Massachusetts, and in 1996, he opened the first Lumber Liquidators store near Boston, Massachusetts. Tom observed that traditional home improvement and flooring retailers underserved customers in terms of price, selection, product quality and overall value. Tom began working directly with vendors and mills to provide customers with broad, high-quality assortments at everyday low prices including in premium categories. He also identified the opportunity to better serve customers by employing knowledgeable sales staff to educate the customer about the product and provide advice on self-installation or working with contractors. In August 1996, Tom opened the second Lumber Liquidators store in Hartford, Connecticut, starting our company s national expansion. In 2000, we opened a central warehouse in Virginia and started operating our own finishing line. We subsequently moved to our current location in Toano, Virginia in 2004. The Toano facility contains our distribution center and finishing line, where we currently finish approximately 70% of our premium Bellawood products. We maintain our in-house finishing capability to ensure product quality and to reduce third-party finishing costs.

We have made a significant investment in developing our national brands, including our portfolio of proprietary product offerings. We believe Lumber Liquidators is now recognized across the United States as a destination for high-quality hardwood flooring at everyday low prices, while our Bellawood brand is known as a premium flooring brand within the industry. We have developed a national store presence, with 111 locations in 42 states as of September 30, 2007. Our stores typically consist of a warehouse and an attached showroom located in industrial or commercial areas that have lower rents than traditional retail locations, are accessible from major roadways and have significant visibility to passing traffic. Our average store is approximately 6,400 square feet, of which approximately 800 square feet is devoted to the showroom selling area. We have designed our stores using a visually appealing and distinctive showroom format to enhance the customer experience while demonstrating our low-cost approach to doing business. Most of our stores have wall racks holding one-foot by two-foot display boards of our flooring products and a warehouse stocked with our most popular hardwood products and high-volume items. Each of our store associates participates in all aspects of our store operations and is trained to understand the characteristics and installation method for the broad range of hardwood floors in order to best educate our customers. We do not, however, provide installation services. We believe that our stores reinforce our customers belief that they get a good deal when they buy from us.

Competitive Strengths

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

Attractive Store Economics

We operate a store model that produces strong returns on investment by combining low capital investment, a small store footprint, minimal staffing and a high average sale of more than $1,750 in 2006. We define average sale as the average invoiced sale per customer, measured on a monthly basis and excluding transactions of less than $250 (which are generally sample orders, or add-ons or fill-ins to previous orders) and of more than $30,000 (which are usually contractor orders). Our average new store across our markets has historically become profitable within three months of beginning operations and returned its initial cash investment within seven months. We estimate that the cost required to open a typical new store is approximately $240,000, of which inventory, net of trade payables, represents approximately $190,000. Our store model targets a pre-tax return on invested capital in excess of 140% for stores open more than three years (including all advertising costs). For the twelve months ended September 30, 2007, we did not have an unprofitable store on a four-wall basis in our portfolio (excluding stores open for less than three months). When measuring profitability on a four-wall basis, we take into account the sales and costs of sales at each individual store, as well as the expenses of that store, which include wages and benefits, rent and local advertising. We do not consider national advertising and store support costs, including those related to corporate overhead and our distribution facility, when calculating profitability on a four-wall basis. We believe the profitability of our store model is driven in part by our ability to carry broad product assortments, while maintaining limited in-store inventories. With the exception of certain high-volume products, we have found that customers typically give us a deposit for their purchases and request delivery of their products approximately one month after placing an order, which reduces our store-level working capital investment requirements and allows us to centrally manage inventory from our distribution facility in Toano. We initiate shipment of most products to a store after an order is placed by a customer, and we can time deliveries to meet our customers specific circumstances. In cases where the customer orders for future delivery, we generally receive a

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50% deposit, which benefits our cash flow and return on investment capital, because we receive immediate partial payment.

Appealing Value Proposition

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

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

Selection. We have developed a broad product assortment of domestic and exotic hardwoods sold under proprietary brands that help us to differentiate our products from those of our competitors. We offer products across a range of price points and quality levels that allow us both to target discrete market segments and to appeal to diverse groups of customers. For example, we sell our Bellawood products to more affluent customers, while our engineered and laminate products are more popular with people seeking more economical flooring solutions.

Quality. We believe that we have achieved a reputation for quality, and that our proprietary brands are recognized for excellence by our customers. We work directly with our supplier mills and brokers to produce flooring that will meet our high quality standards. We require our suppliers to prepare most of the products we sell to our specifications. We also currently finish approximately 70% of our premium Bellawood products at our state-of-the-art Toano facility. We maintain an in-house inspection and quality control function and enforce strict certification requirements for Bellawood supplier mills. As a result, we offer a 50-year residential warranty on our premier Bellawood brand, which we believe is the industry s longest. The multiple coats of natural stains and urethane-based sealers that we apply to Bellawood results in a product with one of the highest scuff resistant finishes in the industry. We monitor the consistency of products produced by our suppliers and work with them to maintain high milling standards.

Availability. Since our founding, we have made it a priority to build long-term relationships with our key supplier mills and brokers. As we have grown, we believe our relationships with our suppliers have strengthened, which we believe helps us ensure our continued access to a broad selection of domestic and exotic hardwood products at attractive prices. In evaluating suppliers, one of the factors we consider is their access to new or hard-to-find species of wood, so that we can continue to expand our range of exotic hardwood products. We also seek out new mills that can meet our demanding standards, and we work with them to evaluate new hardwood species as well as new technologies that may allow us to expand or improve our operations. We believe that these direct supplier relationships are relatively unique in our industry, and offer us a significant competitive advantage. In addition, our centralized inventory at our Toano distribution facility allows us to deliver products not stocked in stores to our customers within a week of purchase or whenever it meets our customers specific needs. Approximately 85% of our merchandise passes through this facility before we move it to our stores. We believe our supply chain and centralized inventory allow us to meet the delivery needs of our customers better than our competitors.

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Established National Brands

We believe both Lumber Liquidators and Bellawood are well-known national brands. We have positioned Lumber Liquidators to represent an attractive value proposition to the customer, and believe we offer superior service and hardwood flooring expertise for customers seeking information about hardwood flooring. Based on our market research, we believe that Bellawood, which accounted for approximately one-third of our 2006 net sales, is among the most-recognized brands in the hardwood flooring industry. We are committed to supporting our brands and products through diverse national marketing campaigns, which have historically included TV, radio and print ads, as well as sports and television show sponsorships, including sponsoring a NASCAR truck racing team and television shows like Extreme Makeover: Home Edition and This Old House, that reach a wide variety of potential customers. In addition, we believe that we benefit from our long-term endorsement relationships with respected and well-known home improvement celebrities such as Bob Vila and Ty Pennington. Bob Vila has been associated with the Bellawood brand for several years, and Lumber Liquidators is the exclusive provider for that product. Ty Pennington, the star of Extreme Makeover: Home Edition, appeals to a younger demographic and is associated with the Lumber Liquidators and Bellawood brands, as well as with the signature Ty Pennington flooring brand that features a Bellawood finish and is sold exclusively through Lumber Liquidators.

Integrated Multi-Channel Sales Model

We have an integrated multi-channel sales model that enables our national store network, call center, website and catalog to work together in a coordinated manner. Due to the average size of the sale, many of our customers conduct extensive research before making a purchase decision. Our sales strategy emphasizes customer service by providing superior convenience and education tools for our customers to learn about our products and the installation process. Customers can view our complete assortment of products through each channel. We believe that potential new customers generally first come to know about us through our national advertising and other marketing efforts. For many of them, the next stop is our website, which provides an informational tool where they can start to learn about our wide variety of products. Our website also allows new customers to see before and after examples from previous customers, explains the installation process and provides product reviews and endorsements. Some customers also contact our call center, which is staffed by more than 50 flooring experts who are also available for online chat and email. Customers can order samples or a catalog through any of our sales channels. Customers who are ready to make a purchase can either visit one of our stores or place an order via our website or call center. We hire store associates who often have relevant industry experience, are able to guide customers through the purchasing process and can provide advice on installation, the selection of a contractor and maintenance. Once an order is placed, customers can either have purchases delivered or can pick them up at a nearby store location. We strive to use our various sales channels to make our customers transactions easy and efficient.

Experienced Management Team with a Proven Track Record

Our senior management team has extensive experience with publicly traded, high-growth retail companies. We believe our company benefits in particular from the leadership of Tom Sullivan, our founder and the chairman of our board of directors, who is a veteran of the specialty hardwood flooring retail business. Under his guidance, we experienced rapid growth and established ourselves as a leading company in the industry. He continues to have an active role in determining our strategic direction and assisting with our day-to-day operations. We believe that his product knowledge and relationships with our suppliers are important competitive advantages. In addition, Jeff Griffiths, our president and chief executive officer, has more than 30 years of experience in the retail industry. He recently served as the president and chief executive officer of videogames retailer Electronics Boutique from 2001 to 2005. Our chief financial officer, Dan Terrell, has more than 15 years of experience working with reporting companies in the retail industry. Over the past two years, we have assembled a management team with

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extensive experience in the specialty retail and hardline retail industries across a broad range of disciplines, including store operations, marketing, merchandising and information systems, production, distribution and finance. We intend to continue to leverage our management team s experience and acumen to execute our strategy effectively. Upon completion of this offering, our executive officers and directors will beneficially own 33% of our company (excluding shares owned by TA Associates funds).

Growth Strategy

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

Expand Our Store Base

The hardwood flooring market is highly fragmented, and we believe there is a significant opportunity to expand our store base. Because of the low capital investment required to open new stores and the attractive returns on investment that our stores generate, we intend to continue to expand our store base. We plan to open at least 25 new stores in total during 2007 and between 30 and 40 new stores during each of the next several years thereafter. As of September 30, 2007, we had opened 20 new stores and had signed leases for seven additional stores during 2007. We believe that we have opportunities to expand our store presence in most of our existing markets, as many of our larger markets have only one or two stores. We also plan to open stores in new markets, leveraging our national advertising campaign, as we believe our store concept has broad national appeal and can be successful in a wide variety of large and small markets.

Improve Existing Store Sales Growth

We seek to drive productivity through strong comparable store sales performance and by improving operational efficiencies. We expect that sales growth will be driven by our investment in our proprietary brands, targeted marketing campaigns and more efficient sales and inventory planning and forecasting. We also expect sales growth will be supported by favorable long-term industry trends, including increasing remodeling activity and consumer preference for hardwood flooring. In addition, we continue to build on what we believe is our strong track record of consistent store-level execution. We intend to maintain our low-cost store model for both our existing and new stores, to focus on increasing gross margins across our assortment of products and to focus on maintaining retail pricing discipline among our stores. We also incentivize our employees using commissions derived from store-level metrics. We plan to increase the number of product shipments from our suppliers directly to our stores, thereby saving delivery time and expense from our Toano facility.

Expand Operating Margins

We attribute our success to our focus on and our ability to deliver on our value proposition to the customer, which results from leveraging our strength as a vertically-integrated, low-cost operator. As we continue to increase our revenues by opening new stores and marketing our proprietary brands, we also plan to decrease marginal costs by taking advantage of improving economies of scale in purchasing, leveraging our existing infrastructure and other fixed expenses, particularly general corporate overhead and lease expenses, and optimizing our finishing, distribution and supply chain management. We believe that we have built out our operations to be able to scale upward to sustain a high level of growth. For example, while we currently operate one finishing line at Toano, which we believe can support our planned growth for at least the next three years, we have the space to construct a second finishing line in the facility that would double our capacity. We believe the second finishing line would require limited incremental investment and could be funded through cash flow from operations. Similarly, we have designed our inventory and management information systems to be scalable as we expand our operations.

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Leverage Brand Marketing Across Multiple Channels

We use our advertising and marketing activities and our multiple sales channels particularly our website and our call center to help educate potential customers about hardwood flooring. As customers learn more about hardwood flooring and how best to shop for it, they also learn more about our products and value proposition, which we believe drives customer store visits and purchases of our products. We believe that as we continue to leverage our multi-channel strategy, we will drive repeat customer traffic. We have also made a significant advertising and marketing investment to link our brands, particularly Lumber Liquidators and Bellawood, to quality and value as well as to establish ourselves as the hardwood flooring experts. We believe that opportunities exist to expand sales with marketing initiatives focused within and across each of our sales channels. For example, in February 2007, we conducted our first mass mailing of catalogs, and we have continued expanding our catalog mailing efforts to prospective customers. Based on our focus group research, we believe that more than 90% of our customers visited our website before making a purchase from us. Initiatives like these should enable us to more cost-effectively reach new customers and encourage previous customers to make additional purchases from us. As we continue to grow and open more stores, we believe that our marketing and branding activities will become more efficient and targeted. We also believe that our customer acquisition costs will decline on both a per-customer and per-store basis.

Our Market

The hardwood flooring market represents approximately 10% of the overall U.S. floor coverings market, which includes carpet and area rugs, hardwood and softwood flooring, ceramic floor and wall tile, resilient sheet and floor tile and laminate flooring. In its 2005 Wood Flooring report, as subsequently updated in March, June and September 2007, Catalina Research estimates that the value of U.S. hardwood flooring wholesale sales in 2005 was approximately $2.3 billion (representing retail sales of $4.1 billion), and, in addition, estimated in November 2005 that the market would grow at a compound annual growth rate of 7.4% through 2011. Despite projected long-term growth, however, Catalina Research estimates that U.S. hardwood flooring sales declined 10.6% in 2006 and declined 14.1% in the first half of 2007 compared to the same period in 2006. Similar declines were estimated across most types of flooring, and were due in particular to decreased new housing demand. The majority of our sales, however, are to consumers engaged in remodeling projects, so despite these market declines, our net sales increased 36% from 2005 to 2006 and 21% from the first nine months of 2006 to the first nine months of 2007. Although we anticipate there may be some volatility in the near term due to decreased housing demand, which Catalina s growth estimate may not fully reflect, we believe we will continue to benefit from several key long-term industry trends and characteristics including:

Increased Home Improvement Spending. Based on the U.S. Census Bureau construction report, residential improvement spending grew at a 7.0% compound annual growth rate from 2000 to 2005. According to the Home Improvement Research Institute, spending on home improvement products is forecasted to grow at a 5.2% compound annual growth rate from 2005 to 2010. The home improvement market is driven by several factors, which include the age of the existing housing stock, home ownership levels, average home size and demographic shifts in the population. We believe home improvement spending is currently being driven in particular by persons engaged in home remodeling projects.

Aging Housing Stock. As homes get older, homeowners remodel in order to maintain habitability, marketability and attractiveness of the home. Also, as homes get older, materials such as floor coverings that were used at the time of initial construction wear out and must be replaced or upgraded to compete with new homes. According to the U.S. Census Bureau, the median age of the U.S. housing stock was 33 years in 2005, which compares to 25 years in 1990 despite record new home construction in recent years.

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Increasing Home Ownership. Data from the U.S. Census Bureau shows that home ownership rates increased to 69% in 2006 from 65% in 1995. Homeowners are significantly more likely to spend on residential improvements than landlords and renters. According to the Joint Center for Housing Studies of Harvard University, homeowners increased their residential improvement expenditures 10% annually from 2000 to 2005, while owners of rental properties have increased their spending by less than 4% annually over the same period.

Increasing Average Size of Homes. As homes have increased in average size, there is more floor surface to be covered. According to the U.S. Census Bureau, the average new single family home was estimated to be 2,434 square feet in 2005, a 16.2% increase from 2,095 square feet in 1995.

Favorable Demographic Trends. Purchases by households with more discretionary income have driven increased hardwood flooring sales. Households with incomes of $70,000 or more made approximately 49.4% of total hardwood surface flooring purchases in 2003, up from 32.8% in 1997. The population segment represented by this income bracket was one of the most quickly growing over the past decade. Similarly, households headed by people between 35 and 64 years of age represented 69.2% of total hard surface flooring purchases in 2003, up from 63.8% in 1997. This segment s population will continue to grow, as the U.S. Census Bureau projects the 45 to 64 age segment to increase to 26.2% of the population by 2010 (up from 22.1% of the population in 2000). This constitutes the largest population increase of any age group over that period.

Evolution of the Hardwood Flooring Market. Manufacturers today offer a wider range of wood species than they have historically, including exotic woods and bamboo, as well as distressed and handscraped flooring lines that appeal to a wider range of consumers. Additionally, manufacturers have designed hardwood flooring that is increasingly easier and less costly to install, such as prefinished, engineered floors that can be installed without glue. Prefinished hardwood floors have become highly prevalent due to ease of installation, multiple styles and applications for situations that in the past precluded the use of hardwood floors. Unfinished products usually require professional installation, sanding and multiple coats of varnish. According to industry sources, the percentage of prefinished square feet of flooring sold increased from 38% in 1999 to 50% in 2004.

Greater Attractiveness of Hardwood Flooring. Hardwood flooring sales have grown historically, and we expect that they will continue to grow as consumer preferences shift to hardwood flooring and as industry innovations drive growth, such as through a greater range of product offerings that appeal to varied consumer preferences and hardwood flooring that has been designed for easier and less costly installation. According to *Floor Focus*, hardwood represented an estimated 14% of the floor covering market in 2006, up from 6% in 1994. We believe that consumers increasingly prefer hardwood flooring for its perceived cosmetic and durability advantages, as well as its ability to contribute to a healthy home because it is relatively easy to clean and traps less dust, dirt and bacteria than some other types of flooring.

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Our Products

We offer a complete assortment of hardwood flooring that includes prefinished premium exotic hardwoods, engineered hardwoods, unfinished hardwoods and laminates. Our product offering is substantially comprised of our proprietary brands, and we plan to offer new proprietary brands in the future. Our hardwood flooring products are generally available in various widths and lengths. They are generally differentiated in terms of quality and price based on the species, grade of the hardwood and quality of finishing as well as the length of the warranty. In total, we offer nearly 350 different flooring product stock-keeping units (SKUs). Brands generally come either prefinished or unfinished. Prefinished floors are finished in a factory under controlled conditions and are ready to be enjoyed immediately after they are installed. Our prefinished products generally have warranties ranging from 10 to 50 years when used in residential settings, and three to five years when used in commercial settings. We check the quality of our prefinished products using a variety of testing methods. Unfinished hardwood flooring is sanded and finished several times after installation, typically by professional flooring contractors. In addition, some brands have specialized features that appeal to particular customer needs. For example, engineered hardwood products are better suited to areas with higher moisture, because they are less affected by changes in humidity. We also offer a broad assortment of flooring enhancements and installation accessories, including moldings, noise-reducing underlay, and adhesives, that complement our assortment of floor offerings.

The graphic below sets forth the percentage of our 2006 net sales that we derived from each product category:

Hardwood

Solid Hardwood. Our proprietary solid hardwood products are milled from one thick piece of wood, which can be sanded and refinished numerous times. We offer flooring products made from more than 25 wood species, including both domestic woods, such as ash, beech, birch, hickory, northern hard maple, northern red oak, pine and American walnut, and exotic woods, such as bloodwood, cherry, cypress, ebony, koa, mesquite, mahogany, rosewood and teak. We offer a 50-year residential warranty, which we believe is the industry s longest, on our premier Bellawood brand (including the Ty Pennington Collection) because the multiple coats of natural stains and urethane-based sealers that we apply to them produce a product with one of the highest scuff resistant finishes in the industry (as measured by the Taber Abrasion Test). In 2006, Bellawood flooring accounted for approximately one-third of our total flooring sales.

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Our proprietary solid hardwood flooring offerings are described in the following table:

Brand	Domestic/ Exotic Wood	Prefinished/ Unfinished	Residential Warranty (years)	SKU Count	Other Characteristics
Bellawood	Both	Prefinished	50	125	Our premium brand; easy to install, with a high-abrasion UV-cured aluminum oxide finish
Ty Pennington Collection	Both	Prefinished	50	5	Unique solid hardwood floors selected by Ty Pennington and featuring a Bellawood finish
Builder s Pride by Dura-Wood	Both	Prefinished	25	40	Solid hardwood for the value-conscious consumer
Virginia Mill Works Co. Handscraped Solid	Domestic	Prefinished	25	9	Handscraped and distressed floors that evoke those found in Colonial American homes
Casa de Colour Collection by Dura-Wood	Domestic	Prefinished	25	35	Solid oak and maple, stained to enhance the natural wood tones
Clover Lea Plantation	Domestic	Both	None	14	Solid pine
R. L. Colston & Sons	Both	Unfinished	None	88	Solid hardwood

Engineered Hardwood. Our proprietary engineered hardwood products are produced by bonding a layer of hardwood to a plywood backing. Like our solid hardwood floors, our engineered hardwood floors are offered in domestic and exotic wood species. All of our engineered hardwood products are prefinished. One brand, Schôn 4 Single Strip Quick Clic, allows for easy-click installation, in which the floors click together and float above the sub-floor instead of being nailed or glued into place. Our proprietary engineered hardwood flooring offerings are described in the following table:

Brand	Domestic/ Exotic Wood	Residential Warranty (years)	SKU Count	Other Characteristics
Schôn Engineered Floors	Both	30	8	Extra-thick solid hardwood wear layer, approved for below-grade installation
Schôn 4 Single Strip Quick Clic	Both	30	19	Floating wood floors featuring single strip boards and easy-click installation
Virginia Mill Works Co. Engineered	Domestic	30	11	Handscraped and distressed floors that evoke those found in Colonial American homes
Timber Top Engineered Wood Floors	Both	15	13	Have a thinner wood top layer; designed for the more value-conscious consumer

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Bamboo and Cork. Bamboo and cork are ecologically friendly choices in flooring that have gained in popularity due to their greater renewability, which we believe appeals to environmentally conscious customers. Bamboo is one of the fastest growing plants and has an extensive root system that creates new bamboo shoots without replanting. Cork flooring, which is durable, acoustical and an insulator, is produced by harvesting the outer bark of the cork oak tree, and the same tree can be harvested numerous times. Our proprietary bamboo and cork flooring offerings are described in the following table:

Brand	Easy-Click Installation	Residential Warranty (years)	SKU Count	Other Characteristics
Schôn Engineered Floating Bamboo Floors	Yes	30	4	Features easy-to-install quick-clic installation and an extra-thick wear layer
Morning Star Bamboo Flooring	No	30	14	Our premier bamboo line, made with 4+ year old bamboo to increase hardness
Ty Pennington Collection	No	30	3	Premium quality bamboo floors selected by Ty Pennington
Lisbon Cork Co. Ltd.	Yes	25	4	Made from real cork; durable; comfortable cushioned surface
Supreme Bamboo by Eco-World Flooring Co.	No	15	4	Designed for the more value-conscious consumer

Laminate. Our proprietary laminate flooring is typically constructed with a high-density fiber board core, inserted between a melamine laminate backing and high-quality photographic paper displaying an image of wood and a ceramic finish, abrasion-resistant laminate top. These products are produced and assembled to our specifications by third parties. Some of our laminate flooring brands allow for easy-click installation or V-groove installation, while others offer a pre-glued undersurface, moisture repellent, soundproofing, single-strip format or a handscraped textured finish. Residential warranties range from 10 to 30 years. We offer various brands and 27 SKUs of laminate flooring in 6mm, 7mm, 8mm and 12mm thicknesses.

Moldings, Accessories and Other Products. We offer a wide variety of hardwood flooring accessories. For example, we sell stair treads and moldings that complement our hardwood floor products. We also sell underlays that can be placed between the new floor and the sub-floor, which insulate sound and cushion the floors. In addition, we sell installation supplies (such as adhesive and trowels), floor cleaning supplies and butcher-block kitchen countertops.

Multiple Integrated Sales Channels

We sell our products through four integrated sales channels, consisting of our stores, call center, website and catalog. We believe that our sales strategy enhances customer service because it provides superior convenience and facilitates the customer s purchasing decision. We provide customers with tools to learn about hardwood flooring and the installation process and give them the ability to view our complete assortment of products through each channel. This integrated process produces operational benefits that improve market penetration and returns on capital.

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Our approach is based on our belief that customers prefer to shop for flooring using multiple channels. Since hardwood flooring is an infrequent purchase for many of our customers, we believe that we increase our chances of making a sale if we are the consumer s choice for expert service at each step of their purchasing decision, from initial education about hardwood flooring to guidance on best maintenance practices for their installed flooring. Our national advertising strategy is designed to raise awareness of our brand and to establish Lumber Liquidators as the first destination for customers who are in the early stages of a purchase decision. Our other marketing efforts, our website and our catalog are similarly designed to both sell products and to provide customers with information throughout the purchasing process. Our research indicates that by the time a customer enters one of our stores, he or she has generally researched our offerings on our website or in our catalog and is ready to make a purchase.

Customers can purchase our products in our stores, or through our call center or website, and can either have those purchases delivered directly to their homes or arrange to pick them up at a nearby store location. With the exception of certain high-volume products, we have found that customers typically expect to take delivery of their products approximately one month after placing an order. Customers who do not take immediate delivery must generally leave a deposit of approximately 50% of the retail sales amount, with the balance payable when the products are delivered. The prices available on our website and from our call center are the same as the prices in our stores.

Stores

We have developed a national store presence, with 111 locations in 42 states as of September 30, 2007. Most of our stores are currently located in primary or secondary metropolitan areas, but we have also succeeded in a number of smaller markets. At present, we generally have no more than two stores in each major metropolitan market, and there are many small and medium-sized markets where we have no stores at all. In identifying new markets, we intend to target selected markets that have demographic and other characteristics similar to those where we have been successful and fill in larger markets with additional stores.

In 2006, our stores that had been open for more than twelve months had average per-store sales of $4.2 million, and we have experienced strong comparable store sales in each of the last four years. Our stores are designed to reflect our low-cost approach to doing business, and consist of a large warehouse and a small attached showroom. The average size of our stores is approximately 6,400 square feet, of which approximately 800 square feet is dedicated to the showroom selling area. We seek buildings that are typically located in industrial or commercial areas that have lower rents than traditional retail locations, are accessible from major roadways and have significant visibility to passing traffic. We enter into short leases, generally for terms of five years, to maximize our real estate flexibility. Our store model targets a pre-tax return on invested capital in excess of 140% for stores open more than three years (including all advertising costs). For the twelve months ended September 30, 2007, we did not have an unprofitable store on a four-wall basis in our portfolio (excluding stores open for less than three months).

We have engaged a national broker to assist us with identifying locations for new stores and negotiating with landlords. After the broker has identified a new site, members of our management team visit the site, and it is reviewed for final approval by our real estate committee. Our first priority is to expand into markets in which we currently do not have a store, or where our existing store is more than an hour s drive away from what we believe is a critical mass of potential customers. We also focus on high density markets that we feel can support multiple stores. In the past, the size of our stores has varied depending on our ability to acquire space opportunistically, but we expect that new stores will generally be between 5,000 and 8,000 square feet, with approximately 800 square feet dedicated to the showroom and the remaining space used as a warehouse.

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The table below highlights certain information regarding our stores open during each of the five years ended December 31, 2006 and the nine months ended September 30, 2007.

	2002	2003	2004	2005	2006	Nine Months Ended September 30, 2007
Number of stores at beginning of period	23	25	40	57	76	91
New stores	2	15	17	19	16	20
Closed stores(1)					(1)	
Number of stores at end of period	25	40	57	76	91	111

(1) The 2006 closed location represents a laminate flooring-only store established to operate during the remaining lease period of a relocated store.

Consistent with our low-cost focus, the layout of our stores is simple and includes design elements that consumer research suggests influence purchasing decisions. Our store design is intended to be both informative and functional. For example, wall displays in our stores show a selection of one-foot by two-foot displays of our flooring products, while the floors are generally laid with various examples of the hardwood flooring products we carry. Our research shows that customers correlate our simple, functional store designs and locations outside of high-rent retail areas with a belief that they have received good value for the money they have spent on our products.

A typical store that has been open for more than 12 months is staffed by a store manager and two assistant managers. We hire additional staff to the extent required by a store s level of business. The store manager is responsible both for store operations and for overseeing our customers shopping experience. Many of our store managers have previous retail experience with large retailers in the home improvement industry, the retail flooring industry or the flooring installation industry. Store manager compensation consists of a base salary and commissions.

Average store inventory is approximately $365,000 and consists of both in-stock inventory and order-specific inventory. Our in-stock inventory is generally comprised of high-volume merchandise that our customers prefer to have available at the time of purchase. Products in this category include laminates, bamboo and certain accessories. We stock most of our other products at our Toano distribution facility, from which we can deliver products to our customers across the country within a week.

We expanded our store base by 19 stores in 2005 and 16 stores in 2006. We plan to open at least 25 new stores in total during 2007 and between 30 and 40 new stores during each of the next several years thereafter. As of September 30, 2007, we had opened 20 new stores and had signed leases for seven additional stores in 2007. We intend to continue to expand our store base in the future. Since we began operations, we have closed only one location, a laminate flooring-only store established to operate during the remaining lease period of a relocated store. Our average new store across our markets has historically become profitable within three months of beginning operations and returned its initial cash investment within seven months.

Call Center

More than 50 flooring experts cross-trained in sales, customer service and product support staff our call center. In addition to receiving telephone calls, our call center staff has recently been made available to chat online with visitors to our website, respond to e-mails from our customers and engage in telemarketing activities. Customers can contact our call center to place an order to be delivered directly

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to their home or picked up at a nearby store, to make an inquiry or to order a catalog. Callers can also order flooring samples for a nominal fee that is credited towards their first purchase. Our call center uses a scalable Internet-based telephone system that allows for rapid movement of our telephone handsets as needed to any available Internet connection. Our call center staff work on a commission basis. Call center sales fulfilled through our Toano distribution facility are credited to the call center, while those picked up at one of our stores are credited to that store. If the sales credited to the various stores were instead credited to our call center, our call center would constitute our largest store by sales volume.

Website

Our website (www.lumberliquidators.com) serves both to educate consumers and to generate sales, whether through a store, our call center or directly via the website itself. Potential customers want information about the products they are considering, and we seek to provide them with what they need to make an informed decision. Visitors to our website can interact with our flooring experts via live chat and can search through a large database of frequently asked questions we call Flooring 101. We also offer product reviews and an extensive before and after gallery from previous customers, as well as detailed product information and how-to videos that explain the installation process. As with our call center, visitors can also order flooring samples. We have included endorsements by Bob Vila and Ty Pennington on the website to add credibility to our message. As part of our effort to distinguish the brand, we also maintain separate websites specifically for Bellawood (www.bellawood.com) and the Ty Pennington collection (www.tyscollection.com), where customers can go to learn more about those product lines and which direct them to our website or our call center if they want to place an order.

Our Lumber Liquidators website was ranked as one of the top 50 retail websites of 2007 by an Internet industry source. Hitwise, a leading online analytics service, consistently ranks our website first relative to our specialty flooring competitors in overall sessions, page views and visit duration, based on their monthly analysis of several of our larger specialty competitors. Hitwise statistics also indicate that traffic is roughly split between men and women, with persons within the ages 25-34 and 35-44 each constituting approximately 25% of website visitors, and more than half of our visitors coming from households with annual incomes greater than $60,000. In 2007, our website averaged more than 650,000 sessions per month through September 30, 2007, with approximately one out of every seven of our website visitors viewing the store locator page. In 2006, we began a concerted effort to collect the names and email addresses of customers who visit our website so as to better serve their needs and to assist us in marketing our products to them. We had collected approximately 500,000 mailable addresses as of September 30, 2007.

Catalog and Other Mailings

Our direct mail strategy focuses on regular contact with our customers and the targeting of prospective purchasers. We distribute our catalog, as well as other direct mailings, to key consumer and commercial segments around specific store locations. Copies of our catalog can also be obtained through our stores, our call center and our website. Our catalog supports in-store, call center and website sales, and approximately 70% of customers who purchased hardwood flooring from us during 2006 had requested a catalog from us. In February 2007, we conducted our first mass mailing of catalogs, in which we mailed approximately 1.5 million catalogs to former customers and others who had provided us with contact information. Response to that program led us to mail 1.5 million postcards in April, 1.5 million catalogs in May and another 1.5 million catalogs in September. In the first nine months of 2007, we also fulfilled 750,000 catalog requests either by handing catalogs out at a store or mailing them directly to the recipient s home. We believe these mailings contributed to an increase in store traffic and call center volume that led to more sales. We expect to continue expanding our catalog mailing efforts to prospective customers in markets where we have stores.

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Customers

We seek to appeal to customers who desire a high-quality product at an attractive value, and are willing to travel to less convenient locations to get it. We sell our products principally to existing homeowners, who represent about 80% of our customer count. Historically, these homeowners are in their mid-30 s or older, are well-educated and have been living in their homes for at least several years. Almost 50% of hardwood surface flooring purchases are made by households with incomes of $70,000 or more. We have found that homeowners like various aspects of wood floors, including appearance and durability, ease of installation, renewability of resources and increasingly higher quality of engineered and laminate flooring. The majority of these customers hire a third-party installer to put in their flooring, with the remainder being do-it-yourself installers. Most of our other sales are to contractors, who are primarily small businesses that are either building a small number of new homes or have been hired by an owner to put in a new floor.

Customer Service and Sales Force

We position ourselves as hardwood flooring experts and believe our high level of customer service reflects this positioning. Key elements of our service include providing consumers with useful product information and answering their hardwood flooring questions, ensuring product availability, following through on customer requests and selling high-quality products at an attractive value. Our store associates are familiar with all aspects of our store operations, and along with our call center staff, are trained to understand the characteristics and installation method for the broad range of hardwood flooring as well as guiding customers through the purchase process. Many of our staff have relevant industry experience, and we are currently developing a formal standardized training program for all of our store associates. We actively participate in local trade shows and home and garden shows, which we find to be an excellent opportunity to educate consumers about our products and distribute our catalogs and samples. Our website has a large frequently asked questions section, and potential hardwood flooring consumers can obtain live assistance through our online chat feature. Consumers can also access how-to videos and slideshows that provide detailed instructions on how to choose and install hardwood flooring.

While we generally do not provide or arrange flooring installation, nor do we generally recommend or endorse installers or installation companies, as a courtesy to our customers, each of our stores maintains a list of local third-party flooring installers that they may provide to customers. In August 2007, we began to work with a national installation company that will be either our exclusive or recommended installer at a number of stores we plan to open in 2007. Depending on the success of this program, we may expand it to other stores in the future. Even in these limited circumstances, however, choosing an installer remains the sole responsibility of the purchaser or homeowner, and we disclaim any liability for the work performed (or any damage caused) by any installer, including those on any list our stores may provide.

Marketing and Advertising

We believe that our marketing and advertising supports our position as the hardwood flooring experts and as the specialty retailer that offers the broadest high-quality selection at everyday low prices. We have structured our marketing and advertising strategy to correspond with our understanding of the purchase cycle associated with hardwood flooring. Based on our market research, we believe that prospective customers generally do not buy on impulse. Instead, they invest time prior to their purchase to learn about hardwood flooring generally and to identify the correct hardwood flooring for their home. Accordingly, our marketing strategy emphasizes product credibility, brand awareness, customer education and direct selling.

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We believe that we establish product credibility primarily through the strength of our product and the attractiveness of our pricing. We believe that we have achieved a reputation for quality and low prices, and that our proprietary brands are recognized for excellence by our customers. Our objective is to sell high-quality products at an attractive value, and we offer a large selection of hardwood flooring year-round at everyday low prices, ranging in quality from our premium Bellawood brand to our more economical brands. We try to avoid being perceived as a volume-driven discounter, so while our promotional cycle focuses on particular buying cycles, we generally try to hold our sales around events where we can create some excitement among customers. For example, we hold sales when we acquire bulk amounts of inexpensive inventory where we can pass along the savings, during three-day weekends when a customer has more time to consider (and possibly even install) a new flooring purchase, and during our annual odd lot sidewalk sale in April. In addition, as part of our efforts to optimize inventory levels, we implemented additional price discounts with respect to slower-moving inventory, primarily during the fourth quarter of 2006.

Our product credibility also benefits from celebrity endorsements and product placement opportunities, and we have long-term endorsement arrangements with respected and well-known home improvement celebrities Bob Vila and Ty Pennington. Bob Vila in particular has been associated specifically with our premium Bellawood proprietary brand for several years. Ty Pennington has endorsed both the Lumber Liquidators and Bellawood brands and has his own hardwood flooring collection, the Ty Pennington Collection. We also co-sponsor various television shows such as Extreme Makeover: Home Edition and HGTV s Dream Home, which use our products and enable potential customers to see both what our flooring will look like after installation and the relative ease with which it can be installed.

We increase brand awareness in a variety of ways, including both advertising and by demonstrating to customers our unique value proposition. We believe that our Lumber Liquidators brand is positioned based on three primary attributes selection, price and service while our Bellawood brand is known as a premium flooring brand within the industry. Over the last few years, we have invested significantly to build awareness and demand for all of our proprietary brands. To increase brand awareness, we conduct ad campaigns on both a national and local level using both traditional and new media. Our activities include:

- buying ads in national and local publications, such as home and garden magazines and local newspapers;

- using targeted television advertising on cable networks such as HGTV, TLC, DIY Network and A&E Network, co-sponsoring television shows like This Old House and securing product placement on television shows like those noted above;

- advertising on syndicated radio programs such as The Rush Limbaugh Show and various programs on National Public Radio;

- engaging in sports marketing by sponsoring the truck driven by Todd Bodine (the 2006 NASCAR Craftsmen Truck Series champion) and engaging in marketing opportunities with Major League Baseball and the National Basketball Association;

- engaging in banner advertising on the Internet, sponsoring links on well-known search engines, having storefronts with large e-tailers and having a large network of online affiliate partners; and

- supporting charitable causes and local communities, including support for Habitat for Humanity, Tomorrow s Children Fund, the National Braille Press and Homes For Our Troops.

We believe our national advertising campaigns have been successful, and we expect to see greater returns on our investment in national advertising as more stores open near people who have already been

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introduced to our brands. We expect to place a greater focus on local advertising to support targeted store growth while maintaining appropriate levels of national advertising. We believe that the percentage of our revenues devoted to marketing and advertising will decline as we continue to expand.

We strive to educate the customer in a variety of ways, including through our website, our catalog and our employees (both in the store and at external events, like trade shows). We also use a variety of mechanisms that directly support sales and focus on identifying new prospective customers and contacting known prospective customers to encourage them to make a purchase. Many of these require the potential customer to opt in, which we believe increases our response rate. For example, we send emails to our past customers and self-identified prospective customers, and we employ opt-in sweepstakes with major brands such as HGTV and TLC. We also distribute our catalog and other direct mailings throughout the year to key consumer and commercial segments targeted around specific store locations, and engage in telemarketing campaigns.

Suppliers

We work directly with a select group of vendors and mills with whom we have cultivated long-standing relationships to ensure a consistent supply of high-quality product at the lowest prices. As part of ensuring the high-quality nature of our brands, we have developed demanding product standards. As we have grown, we believe our supplier relationships have strengthened, which we believe helps to ensure our access to a broad selection of products. Many suppliers have grown to support our business. We select suppliers based on a variety of factors, including their ability to supply products that meet industry grading standards and our specifications. As part of ensuring that they are meeting relevant standards, we inspect samples, make periodic site visits to our suppliers mills and selectively inspect inbound shipments at our distribution center. Based on our historical experience, we believe that some of the mills that we use are among the best in their respective markets. We also support social and environmental responsibility among our supplier community, and the majority of our suppliers have entered into an environmental and social responsibility agreement with us. This agreement contains a code of conduct regarding our expectations concerning environmental, labor and health and safety matters. We encourage the use of renewable resources, and generally prefer to use suppliers that operate in areas where the harvest rate is slower than tree planting and growth rates.

We currently purchase products from approximately 90 vendors. We primarily purchase flooring directly from mills and trading companies. In 2006, 68% of our hardwood merchandise was purchased directly from mills, 31% was purchased from trading companies and 1% of our product was purchased through buying agents. Trading companies contract with mills to make products for us, and handle certain shipping and customs matters. In 2006, one of our suppliers, Sequoia Floorings, accounted for approximately 14% of our purchases, and acted as agent for another of our suppliers that accounted for another 7% of our purchases. Including those companies, our top 10 suppliers account for approximately 63% of our supply purchases in 2006. We believe that we are one of the largest customers for most of our largest suppliers, which we believe enables us to obtain better prices in some circumstances.

We do not have long-term contracts with most of our suppliers, as we believe is standard in our industry, but we believe we have stable long-term historical relationships with the majority of mills with whom we do business. We generally purchase product on an order-by-order basis, and write orders for delivery in 90 to 180 days. We also have one long-term purchase agreement with a trading and import company that we entered into in July 2006. Pursuant to the terms of that agreement, we are required to order a specified minimum amount of product each year, totaling approximately 27 million square feet of product (representing less than 5% of our estimated purchasing needs) over the four-year period of the agreement. The agreement provides for a set menu of products, including prices and specifications, from which we can pick in placing our orders. The agreement also provides for a detailed process by which either party can request a change in prices or specifications, or add or delete products from the menu. Certain disputes have arisen between the parties primarily with regard to product quality, unit price changes and delivery and payment obligations. We are not currently receiving any product under the agreement and we intend to seek payment for our cover costs relating to purchase orders that were not delivered. The products we ordered from the vendor that are not being delivered are available from other suppliers and the cover costs are expected to be immaterial.

Overseas suppliers deliver our product to us by sea, usually requiring between 21 and 35 days from port to port. These products are delivered to a U.S. port of entry, most frequently Norfolk, Virginia, after which the majority is shipped to our Toano distribution facility for finishing (when required) and distribution to our stores. The balance is shipped directly from the port of entry to our stores. Products supplied by our North American suppliers are generally delivered to our Toano facility or our stores by truck. Our Toano facility is strategically located near the international shipping port in Norfolk, Virginia and major east-west and north-south interstate highways. In 2006, approximately 30% of our product was sourced from Asia, approximately 24% was sourced from South America, approximately 35% was sourced from North America and 11% was sourced from other locations. All of our foreign purchases are negotiated and paid for in U.S. dollars.

Although we maintain strong relationships with our suppliers, we believe that opportunities exist to improve purchasing terms in the future. In evaluating suppliers, one of the factors we consider is their access to new or hard-to-find species of wood, so that we can continue to expand our range of exotic hardwood products. We also seek out new mills that can meet our standards, and we work with them to evaluate new hardwood species and new technologies that may allow us to expand or improve our operations. We continually seek out new suppliers to ensure that we have sufficient product flow to support our current operations and expected growth. We believe that alternative and competitive suppliers are available for most of our products.

Finishing

We finish more than 20 million square feet of prefinished hardwood flooring annually at our state-of-the-art finishing facility in Toano. This includes approximately 70% of all Bellawood products, the balance of which we obtain from qualified prefinishing suppliers in both North and South America. We also finish small quantities of certain of our other products at that facility. The Toano finishing facility sources both domestic and exotic unfinished flooring from more than 20 mills, trading companies and buying agents located in North and South America, Asia and Australia. We currently operate one finishing line at Toano and we have the space to construct a second finishing line in that facility. We continually invest in improving our process controls and product quality, and we believe that our existing finishing infrastructure at our Toano facility can support our planned growth over at least the next three years. We believe the incremental investment to fund a second finishing line at our Toano facility will be limited and can be funded through cash flow from operations.

At our Toano facility, we prefinish the hardwood flooring to produce a product that has one of the highest scuff resistant finishes in the industry as measured by the Taber Abrasion Test, an abrasion testing method designed to measure the abrasion resistance of protective floor finishes. The prefinishing process involves several steps. We begin the process by sanding the unfinished hardwood to ensure that it has uniform thickness and optimal smoothness. We then apply multiple coats of natural stains and urethane-based sealers to enhance grain appearance and provide excellent abrasion resistance and toughness. Each coat is cured to ensure proper adhesiveness to the hardwood, and the wood is scuffed with denibber brushes between coats to ensure smoothness. Finally, we apply a topcoat, which provides scratch and stain resistance, further enhances abrasion resistance and controls the final gloss or sheen of the hardwood flooring. The topcoat is then cured and cooled, and the prefinished hardwood is graded and boxed.

We have adopted sophisticated quality assurance policies and techniques, which are based on national and international standards where appropriate. These standards specify requirements for flooring products, sampling techniques and other quality-related activities, and are published by organizations

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such as the National Wood Flooring Association, the National Oak Flooring Manufacturers Association and the International Organization for Standardization.

Throughout the prefinishing process, we perform numerous tests and visual inspections to verify that the flooring complies to our specifications, that we are maintaining effective control over the finishing process and that the final prefinished hardwood flooring meets our requirements. In developing these policies and techniques, we emphasize defect prevention, minimizing variations in our products, decreased waste and workplace safety. For example, samples of each of our products undergo Taber Abrasion Testing. As part of the testing process, flooring is secured to a turntable that is a weighted wheel covered in sandpaper. The turntable is rotated, causing the sandpaper to wear against the finish. Each full revolution is counted as a Taber cycle, and the number of rotations that it takes the sand paper to get through the finish becomes the Taber rating for that finish.

Distribution, Order Fulfillment and Inventory Management

We operate a single distribution center located in Toano, Virginia. We warehouse our products at that facility before shipping them to our stores by truck, and approximately 85% of our merchandise passes through this facility before we move it to our stores. It generally takes between two to five days for a shipment to reach our stores, and each store receives an average of 1.4 shipments per week. In some cases, our suppliers deliver products directly to our stores. We believe that our existing distribution infrastructure at our Toano facility can support our planned growth over at least the next three years. We continually monitor our operations to identify opportunities to improve efficiencies, and are currently working with a consultant to improve the efficiency of our operations and plan for future growth.

In the first quarter of 2007, we upgraded our corporate network with high-speed dedicated lines capable of carrying both voice and data communications. At this time all of our stores were rewired for voice and data. Voice communications are now carried over a scalable Internet-based network. Before the end of 2007, we plan to implement a new point-of-sale system in all of our stores. This touch screen system provides for real-time tracking of inventory and sales information. We believe that our updated inventory management and communications systems will allow for improved forecasting, more efficient inventory management, rapid stock replenishment and concise merchandise planning. We believe that these systems will give us substantial flexibility as we grow.

Competition

We are the largest specialty retailer of hardwood flooring in the United States, and compete in a hardwood flooring market that is highly fragmented. We compete on the basis of price, quality, selection and availability of hardwood flooring we offer our customers, as well as the level of customer service we can provide. Our competitive position is also influenced by the availability, quality and cost of merchandise, labor costs, finishing, distribution and sales efficiencies and our productivity compared to that of our competitors. The market includes both national and regional home improvement chains which specialize in the lower-end, higher-volume flooring market and offer a wide range of home improvement products other than flooring. We also compete against smaller national specialty flooring chains, some of which have an Internet presence, and a large number of local and regional independent flooring retailers, including a large number of privately-owned single-site enterprises.

We estimate, based on internal market research, that our share of the hardwood flooring retail market was approximately 6% in 2006, up from approximately 4% in 2005. We believe that we compete effectively against the large national chains by offering competitive prices, higher-quality hardwood flooring products, a broader product assortment, a shorter delivery time, and better customer service by virtue of our more knowledgeable sales staff and single-product focus. In addition, we believe that our largest competitors with Internet operations focus to a greater extent on the lower-priced segment of the

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hardwood flooring market, particularly engineered, bamboo and laminate flooring. The remainder of the hardwood flooring market is dominated by small local independent retailers that usually sell carpet and tile in addition to hardwood flooring. Most of these retailers purchase their hardwood flooring from domestic manufacturers or distributors, and typically do not stock hardwood flooring, but order it only when the customer makes a purchase. As a result, we believe it takes these retailers longer than us to deliver their product to customers, and their prices tend to be higher than ours.

We also compete against companies that sell other types of floor coverings, such as carpet, vinyl sheet and tile, ceramic tile, natural stone and others.

Employees

As of December 31, 2006, we had 490 employees, 96% of whom were full-time and none of whom was represented by a union. Of these employees, 57% work in our stores, 22% work in corporate or similar functions (including our call center employees) and 21% work in our finishing and distribution operations. As of September 30, 2007, we had 651 employees, of whom 64% work in our stores, 17% work in corporate or similar functions and 19% work in our finishing and distribution operations. We believe that we have good relations with our employees.

Properties

As of September 30, 2007, we operated 111 stores located in 42 states. Our stores average approximately 6,400 square feet, of which an average of 800 square feet is dedicated to the showroom and the remainder used as a warehouse. As of September 30, 2007, we had opened 20 new stores and had signed leases for seven additional stores (which, since they are not yet operational, are not included in the table below) in 2007. Our Toano, Virginia finishing and distribution facility has 307,784 square feet, of which approximately 32,000 square feet are office space, and is located in on a 74-acre plot. We currently operate one finishing line at Toano, and we have the space to construct a second finishing line in that facility.

The table below sets forth the locations (alphabetically by state) of our stores in operation as of September 30, 2007.

State	Stores	State	Stores	State	Stores	State	Stores
Alabama	1	Indiana	2	Missouri	1	Oregon	1
Arizona	2	Iowa	1	Nebraska	1	Pennsylvania	4
Arkansas	1	Kansas	1	Nevada	2	S. Carolina	2
California	9	Kentucky	1	New Hampshire	2	Tennessee	3
Colorado	2	Louisiana	2	New Jersey	3	Texas	9
Connecticut	2	Maine	1	New Mexico	1	Utah	1
Delaware	1	Maryland	2	New York	6	Virginia	6
Florida	11	Massachusetts	4	N. Carolina	2	Washington	3
Georgia	2	Michigan	3	Ohio	4	W. Virginia	1
Idaho	1	Minnesota	2	Oklahoma	2	Wisconsin	3
Illinois	2	Mississippi	1				

We lease all of our stores and our Toano finishing and distribution facility. Our store leases generally have an initial operating lease term of five years and most provide options to renew for specified periods of time. A majority of our leases provide for fixed monthly or annual rentals. Certain of our leases include provisions for escalating rent, generally at fixed increases on predetermined dates. Many of our leases require us to pay taxes, insurance and common area maintenance expenses

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associated with the properties. The initial operating lease term for our Toano facility runs through December 31, 2019, with an option to renew for an additional 15-year term. Our Toano lease provides for fixed monthly rent with an annual increase of 3.0%, and it requires that we pay real estate taxes associated with the property, carry certain insurance and maintain the property in good condition and repair.

We currently lease 23 of our store locations and our Toano facility, which includes a store location, from ANO LLC, a company that is wholly owned by Tom Sullivan, our founder and the chairman of our board of directors. Tom is also the sole owner of DORA Real Estate Company, LLC and Wood on Wood Road, Inc., and has a 50% membership interest in BMT Holdings, LLC, and we lease one store location from each of these entities. See Certain Relationships and Related Party Transactions.

Intellectual Property and Trademarks

We have a number of marks registered in the United States, including Lumber Liquidators®, Bellawood®, 1-800-FLOORING®, Dura-Wood®, Blutec®, Quickclic®, Virginia Mill Works Co. Hand Scraped and Distressed Floors®, Morning Star Bamboo Flooring® and Dream Home Laminate Floors® and the Lumber Liquidators design mark, and have applied to register a number of other trademarks, including Builder s Pride , Schön Engineered Floors and other product line names. We have also registered certain marks in jurisdictions outside the United States, including the European Union, Canada, Australia and Japan, and have registration applications pending in several other jurisdictions. We regard our intellectual property as having significant value and these names are an important factor in the marketing of our brands. We are not aware of any facts that could be expected to have a material adverse effect on our intellectual property.

Government Regulation

We are subject to extensive and varied federal, state and local government regulation, including regulations relating to employment, public health and safety, zoning and fire codes. We operate each of our stores and finishing facility and distribution center in accordance with standards and procedures designed to comply with applicable codes and regulations.

Our operations and properties are also subject to federal, state and local laws and regulations relating to the use, storage, handling, generation, transportation, treatment, emission, release, discharge and disposal of hazardous materials, substances and wastes and relating to the investigation and clean up of contaminated properties, including off-site disposal locations. We do not incur significant costs complying with environmental laws and regulations. However, we could be subject to material environmental costs, liabilities or claims in the future, especially in the event of changes in existing laws and regulations or in their interpretation.

Our suppliers are also subject to the laws and regulations of their home countries, including in particular laws regulating forestry and the environment. We consult with our suppliers as appropriate to ensure that they are in compliance with applicable home country laws. We also support social and environmental responsibility among our supplier community, and the majority of our major suppliers have entered into an environmental and social responsibility agreement with us. This agreement contains a code of conduct regarding our expectations concerning environmental, labor and health and safety matters, which includes among its guidelines an understanding that our suppliers must comply with the laws, rules and regulations of the countries in which they operate.

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Legal Proceedings

We are involved in a claim brought by Dr. Clifford Wayne Bassett in the U.S. District Court for the Southern District of New York against us, E.W. Scripps Company (Scripps) and others, in connection with an article we purchased from Scripps, describing the benefits of hardwood flooring in relation to other types of flooring. The article contained a quote by Dr. Bassett, an allergist, who claims the quote was unauthorized. Dr. Bassett has asserted damages in excess of $10 million. The matter is in the early stages of litigation and, while there is a reasonable possibility that a material loss may be incurred, we cannot estimate the loss to us, if any, at this time. We intend to defend vigorously against this claim and, to the extent warranted, to seek contribution or indemnification from other parties.

In July 2007, a former senior executive officer filed a demand for arbitration in connection with his resignation of employment in May 2006. That executive alleges that he terminated his employment for good reason, as defined in his employment agreement and our warrant plan, based on an allegedly substantial reduction in his responsibilities. In his demand for arbitration, the former senior executive contends that we breached our obligations to him upon his resignation of employment. He is seeking damages of approximately $0.7 million (plus the value of certain other specified benefits), as well as a declaration that he has owned 1% of the company since he terminated his employment. An arbitration hearing was held on October 1-2, 2007. The parties will be afforded the opportunity to submit post-arbitration briefs and additional testimony and evidence may be presented. While there is a reasonable possibility that a material loss may be incurred, we cannot estimate the loss to us, if any, at this time. We intend to defend vigorously against this claim.

In addition, we are involved in various claims and legal actions in the ordinary course of business. We do not believe that the ultimate resolution of these actions will have a material adverse effect on our financial position, results of operations, liquidity or capital resources. However, a significant increase in the number of these claims or an increase in amounts owing under successful claims could materially and adversely affect our business, financial condition, results of operations and cash flows.

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MANAGEMENT

Executive Officers and Directors

The following table sets forth information about our executive officers and directors, including their ages as of September 30, 2007.

Name	Age	Position
Thomas D. Sullivan	48	Chairman of the board of directors; Founder (1)
Jeffrey W. Griffiths.	56	President and chief executive officer; Director (2)
Douglas T. Moore	51	Director (1)
John M. Presley	47	Director (1)
Martin F. Roper	44	Director (1)
Richard D. Tadler	50	Director (1)
Macon F. Brock, Jr.	65	Director nominee (3)
Daniel E. Terrell	43	Chief financial officer
E. Livingston B. Haskell	35	Secretary; General corporate counsel
Rick A. Boucher	50	Senior vice president, supply chain
Robert M. Morrison	51	Senior vice president, store operations
Marco Q. Pescara	42	Senior vice president, direct marketing and advertising
Andrew P. Shulklapper	45	Senior vice president, merchandising
Kenneth M. Strohschein	36	Senior vice president, information technology
H. Franklin Marcus, Jr.	62	Vice president, finance; Treasurer
Tyler C. Greenan	38	Vice president, store operations

(1) The parties to the stockholders agreement described below under Certain Relationships and Related Party Transactions agreed to elect to our board one individual nominated by TA Associates Funds, two individuals nominated by Mr. Sullivan and two individuals nominated by Mr. Sullivan who are deemed acceptable by TA Associates Funds. TA Associates Funds selected Mr. Tadler and Mr. Sullivan selected himself among the initial nominees. Messrs. Moore, Presley and Roper were subsequently nominated and elected to the board effective April 2006.

(2) Mr. Griffiths serves on our board pursuant to his employment agreement with us.

(3) Mr. Brock has been nominated to serve on the board, effective the day after this offering closes.

Thomas D. Sullivan is our founder and has been the chairman of our board of directors since our inception in 1994. Prior to September 2006, Mr. Sullivan also served as president and chief executive officer since our incorporation in 1994. Mr. Sullivan serves on the board of directors of Dilon Technologies, LLC and several other privately held companies.

Jeffrey W. Griffiths has been the president and chief executive officer of Lumber Liquidators since September 2006, and a director of Lumber Liquidators since October 2006. Mr. Griffiths was previously the president and chief executive officer of video game retailer Electronics Boutique Holdings Corp. (EB) from 2001 through 2005, when EB merged with GameStop Corp. Mr. Griffiths career at EB spanned more than 20 years. He served as vice president and senior vice president of merchandising, marketing and distribution for EB from 1987 to 1996 and from 1996 to 2001, respectively. Mr. Griffiths also served as a director of EB from 2001 to 2005 and of Game PLC, formerly Electronics Boutique PLC, from 1995 to 1997. Mr. Griffiths holds a B.A. in history from Albright College and an M.B.A. from Temple University. He serves on the board of directors of THQ, Inc., on the board of trustees of Albright College and the board of directors of the Philadelphia Academies Inc.

Douglas T. Moore has been a director of Lumber Liquidators since April 2006. Mr. Moore currently serves as senior vice president, hardlines merchandising for Sears Holdings Corporation in Hoffman

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Estates, Illinois. In this capacity, he is the chief merchant for the appliance, lawn and garden, tools and home electronics businesses for Sears and KMart. Mr. Moore served for 17 years as a senior executive of Circuit City Stores, Inc., with his last position as executive vice president, chief merchandising officer. Mr. Moore has also held operational and consumer marketing positions at AMF Bowling, Inc., A.H. Robins Company, Inc. and the Carnation Company. He received his undergraduate degree and M.B.A. from the University of Virginia.

John M. Presley has been a director of Lumber Liquidators since April 2006. In May 2006, Mr. Presley joined Fifth Third Bancorp in a strategic initiative post, where he is responsible for executing market banking strategies in existing and emerging markets. He previously served as chief financial officer for Marshall & Ilsley Corp. from 2004 to 2006, and was chief financial officer of National Commerce Financial Corp. in Memphis, Tennessee, and president and chief executive officer of First Market Bank in Richmond, Virginia. Mr. Presley holds a B.A. in economics and business administration from Rhodes College.

Martin F. Roper has been a director of Lumber Liquidators since April 2006. Mr. Roper is the president and chief executive officer of The Boston Beer Company, Inc., where he has worked since 1994 and has been a director since 1999. Prior to assuming that position in January 2001, he had served as the president and chief operating officer of that company since December 1999. Mr. Roper holds a B.A. in engineering and M.A. in engineering in manufacturing technology from Cambridge University and an M.B.A. from Harvard Business School. He serves on the board of directors of The Boston Beer Company, Inc.

Richard D. Tadler has been a director of Lumber Liquidators since December 2004. Mr. Tadler is a managing director of TA Associates, Inc. He has been associated with TA Associates, Inc. since 1987, specializing in medical and specialty service businesses. Mr. Tadler holds a B.S. in finance from the McIntire School of Commerce at the University of Virginia and an M.B.A. from the Wharton School of Finance. He is currently a director of several privately held companies and non-profit organizations.

Daniel E. Terrell has been the chief financial officer of Lumber Liquidators since October 2006. Prior to assuming this position, Mr. Terrell served as our controller from November 2004. Mr. Terrell was previously the vice president, controller & credit of Peebles Inc., a specialty apparel retailer that he joined in 1990 and where he continued to work after it was acquired in 2003 by Stage Stores, Inc. Before joining Peebles, Mr. Terrell worked for Ernst & Young. Mr. Terrell holds a B.S. in accounting from Virginia Tech.

E. Livingston B. Haskell has been the secretary and general corporate counsel of Lumber Liquidators since July 2006. Prior to assuming this position, Mr. Haskell was a partner at Williams Mullen and, before February 2006, was an associate at that firm. Mr. Haskell holds a B.S. in finance and marketing from the McIntire School of Commerce at the University of Virginia and a J.D. from Washington and Lee University.

Rick A. Boucher has been senior vice president, supply chain of Lumber Liquidators since July 2007. Prior to assuming this position, Mr. Boucher served more than 22 years with Cadbury Schweppes PLC as the North American vice president of logistics and distribution. Mr. Boucher holds a B.D. in business administration from Niagara College.

Robert M. Morrison has been the senior vice president, store operations of Lumber Liquidators since January 2006. Prior to assuming this position, Mr. Morrison worked at and was part-owner of Morrison/Fleming Solutions from May 2005. Mr. Morrison was also president of Artistic Tile, Inc. from 2004 to 2005 and senior vice president and chief operating officer of Waterworks Inc. from 1999 to 2004. Mr. Morrison holds a B.S. in geology from Michigan State University.

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Marco Q. Pescara has been the senior vice president, direct marketing and advertising of Lumber Liquidators since April 2006. Prior to assuming this position, Mr. Pescara served for more than five years as the vice president of direct response and marketing integration at Hickory Farms, Inc. Mr. Pescara holds a B.S. from the University of Toledo, an M.S. from Boston University and an M.B.A. from the University of Pittsburgh.

Andrew P. Shulklapper has been the senior vice president, merchandising of Lumber Liquidators since February 2007. Prior to assuming this position, Mr. Shulklapper was the division merchandise manager, consumer electronics for Sears Holdings Corporation from 2004 until 2007 and vice president, global market research for Displaysearch from 2003 to 2004. He also worked at Circuit City Stores, Inc. for twelve years, and the last position he held there was division merchandise manager for consumer electronics. Mr. Shulklapper holds a B.A. in economics from the University of Vermont.

Kenneth M. Strohschein has been the senior vice president, information technology of Lumber Liquidators since February 2006. Prior to assuming this position, Mr. Strohschein worked for Hickory Farms, Inc. from 2003, where he served as vice president of management information systems, chief information officer of that company from 2004 to 2006. Mr. Strohschein also worked for ten years at Busch s Incorporated, a supermarket chain where, among other positions, he served as director of information technology for eight years. Mr. Strohschein holds a B.S. in management information systems from Kennedy-Western University.

H. Franklin Marcus, Jr. has been the vice president, finance and treasurer of Lumber Liquidators since October 2006. Prior to assuming this position, Mr. Marcus served as our chief financial officer from 2001 to 2006 and our secretary from 2004 to 2006. Mr. Marcus holds a B.S. in accounting from the McIntire School of Commerce at the University of Virginia.

Tyler C. Greenan has been the vice president, store operations of Lumber Liquidators since 2003. Prior to assuming this position, Mr. Greenan served as a regional manager and our vice president of store operations from 1998. Mr. Greenan holds a B.A. from the University of Miami.

Set forth below is a brief description of Mr. Macon F. Brock, Jr., who we expect will become a director effective the day after this offering closes:

Macon F. Brock, Jr. has been nominated to serve as a director, effective the day after this offering closes. Mr. Brock is a founder of Dollar Tree Stores, Inc. He served as the President of Dollar Tree from 1986 until 2001 and as Chief Executive Officer from 1993 until 2003. He has been a director of Dollar Tree since 1986 and Chairman of the Board since 2001. Until 1991, Mr. Brock was an officer and director of K&K Toys, Inc. Mr. Brock is Chairman of Randolph-Macon College. Mr. Brock also serves on the boards of directors of several smaller privately held companies and non-profit organizations. Mr. Brock earned his B.A. from Randolph-Macon College and served as a Captain in the U.S. Marine Corps. He was a special agent for U.S. Naval Intelligence before entering the retail business.

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Board of Directors

Board Structure

We currently have six directors. We have nominated Macon Brock to serve on the board, effective the day after this offering closes. All members of the board are elected annually. In connection with this offering, we will change the structure of the board and the method of electing directors. The board will be divided into three classes, as nearly equal in number as possible, serving staggered terms. About one-third of the board will be elected annually. See Description of Capital Stock Certain Certificate of Incorporation and Bylaw Provisions. Our board has determined all of our directors other than Messrs. Sullivan, Griffiths and Tadler (for purposes of the audit committee only) meet the independence requirements of the New York Stock Exchange and the federal securities laws.

Board Committees

Prior to this offering, our board of directors will establish standing committees in connection with the discharge of its responsibilities. These committees will include an audit committee, a compensation committee and a nominating and governance committee. The board of directors will also establish such other committees as it deems appropriate, in accordance with applicable law and regulations and our certificate of incorporation and bylaws.

Audit Committee. Prior to this offering, our board of directors will establish an audit committee, which is expected to consist of Messrs. Presley (chair), Moore and Roper, to assist our board in overseeing the preparation of our financial statements, the independent registered public accounting firm s qualifications and independence, the performance of our internal audit function and independent registered public accounting firm and our compliance with legal and regulatory requirements. Within a year of this offering, all of the members of the audit committee will be independent, as determined in accordance with the rules of the New York Stock Exchange and any relevant federal securities laws and regulations. Immediately following the offering, we expect that at least one member of the committee will be independent, as permitted by the relevant transition rules.

Compensation Committee. Prior to this offering, our board of directors will establish a compensation committee, which is expected to consist of Messrs. Roper (chair), Tadler and Brock. Within a year of this offering, all of the members of the compensation committee will be independent, as determined in accordance with the terms of the New York Stock Exchange and any relevant federal securities laws and regulations. Immediately following the offering, we expect that at least one member of the committee will be independent, as permitted by the relevant transition rules. The compensation committee will have overall responsibility for evaluating and approving our executive officer incentive compensation, benefit, severance, equity-based or other compensation plans, policies and programs. The compensation committee will also produce an annual report on executive compensation for inclusion in our proxy statement.

Nominating and Governance Committee. Prior to this offering, our board of directors will establish a nominating and governance committee, which is expected to consist of Messrs. Moore (chair), Presley and Brock. Within a year of this offering, all of the members of the nominating and governance committee will be independent, as determined in accordance with the rules of the New York Stock Exchange and any relevant federal securities laws and regulations. Immediately following the offering, we expect that at least one member of the committee will be independent, as permitted by the relevant transition rules. The nominating and governance committee will assist our board of directors in implementing sound corporate governance principles and practices. Our nominating and governance committee will identify individuals qualified to become board members and recommend to our board of directors the director nominees for the next annual meeting of shareholders. It will also review the

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qualifications and independence of the members of our board of directors and its various committees on a regular basis and make any recommendations the committee members may deem appropriate from time to time concerning any recommended changes in the composition of our board.

Limitation of Liability and Indemnification

Our certificate of incorporation and bylaws will limit the liability of directors to the maximum extent permitted by Delaware law. Specifically, a director will not be personally liable for monetary damages for breach of fiduciary duty as a director, except liability for:

- any breach of the director s duty of loyalty to us or our shareholders;
- acts of omissions not in good faith or which involve intentional misconduct or a knowing violation of law;
- unlawful payments of dividends or unlawful stock repurchases or redemptions; or
- any transaction from which the director derived an improper personal benefit.

Our bylaws will provide that we will indemnify our directors and officers and may indemnify our employees and other agents to the fullest extent permitted by law. We believe that indemnification under our bylaws will cover at least negligence and gross negligence on the part of indemnified parties. Our bylaws will also provide that we will advance expenses incurred by a director or officer in advance of the final disposition of any action or proceeding, and we may advance expenses incurred by our employees or other agents in advance of the final disposition of any action or proceeding. Our bylaws will also permit us to secure insurance on behalf of any officer, director, employee or other agent for any liability arising out of his or her actions in his or her capacity as an officer, director, employee or other agent. We have in the past and may in the future enter into agreements to indemnify our directors, executive officers and other employees as determined by the board of directors. These agreements will provide for the indemnification of directors and officers to the fullest extent permitted by Delaware law, whether or not expressly provided for in our bylaws, and govern the process by which claims for indemnification are considered. We believe that these bylaw provisions and indemnification agreements are necessary to attract and retain the services of highly qualified persons as directors and officers.

The limited liability and indemnification provisions in our certificate of incorporation, bylaws and indemnification agreements may discourage shareholders from bringing a lawsuit against our directors for breach of their fiduciary duty and may reduce the likelihood of derivative litigation against our directors and officers, even though a derivative action, if successful, might otherwise benefit us and our shareholders. A shareholder s investment in us may be adversely affected to the extent we pay the costs of settlement or damage awards against our directors and officers under these indemnification provisions.

There is no pending litigation or proceeding involving any director, officer or employee where indemnification is sought, nor are we aware of any threatened litigation that may result in indemnification claims.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted for directors, officers and controlling persons of us under the foregoing provisions or otherwise, we have been informed that, in the opinion of the SEC, such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable.

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Compensation Committee Interlocks and Insider Participation

None of the members of our compensation committee, once it is formed, will be or have ever been an officer or employee of us. None of our executive officers serves or has served as a member of the board of directors, compensation committee or other board committee performing equivalent functions of any entity that has one or more executive officers serving as one of our directors or on our compensation committee.

Director Compensation

For 2006, directors who are also our employees, as well as Mr. Tadler, did not receive compensation for their service on our board of directors or any board committee. Each of our other non-employee directors received an annual retainer fee of $15,000, payable quarterly in increments of $3,750, beginning in the quarter in which they were elected. The three non-employee directors who received such compensation (Martin Roper, Douglas Moore and John Presley) were elected effective April 26, 2006, so each received an annual retainer fee of $11,250. This retainer fee covers annual services, including participation in up to six board meetings. If Messrs. Roper, Moore and Presley attended more than six meetings during the year, they would have been entitled to receive meeting fees of $2,500 per meeting attended in person or $1,000 per meeting attended by telephone. Each of Messrs. Roper, Moore and Presley also received options to purchase 26,385 shares of our stock at an exercise price of $7.58 per share (which, based upon management s estimate, was the fair market value of a share of our stock on the date the options were granted). Directors have also been reimbursed for expenses incurred in connection with their service as directors, including travel expenses for meeting attendance.

Upon consummation of this offering, directors who are also our employees will continue to receive no compensation for their service on our board of directors or any board committee. We expect to pay all of our non-employee directors (including Mr. Tadler) annual retainer fees and additional fees for attendance at board meetings in excess of six per year, and making annual option grants to our non-employee directors under our 2007 Plan, in each case in the amounts set annually by the board of directors. While the final amounts have not yet been determined by the board, we currently expect that each non-employee director will receive an annual cash retainer of $25,000 and an annual grant of restricted stock units with a one-year vesting period, in an amount to be set based upon the closing price of our common stock at the end of the day on which we hold our annual shareholder s meeting, but not to exceed a value of approximately $65,000. We expect that directors will be given the opportunity to take the cash portion of their retainer in company stock. Annual retainers are expected to be paid to the chairperson of each committee of the board of directors as follows: $15,000 for the audit committee chairperson, $7,500 for the compensation committee chairperson and $5,000 for the nominating/governance committee chairperson. Annual retainers are also expected to be paid to committee members as follows: $7,500 for the audit committee, $3,750 for the compensation committee and $2,500 for the nominating/governance committee. Directors will also be reimbursed for expenses incurred in connection with their service as directors, including travel expenses for meeting attendance. We intend to continue to reimburse promptly all non-employee directors for reasonable expenses incurred to attend meetings of our board of directors or board committees. Other than as described above, we do not expect to provide any of our directors with any other compensation or perquisites.

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The following table sets forth compensation paid to our directors in their capacities as such in the fiscal year ended December 31, 2006.

Name	Fees Earned or Paid in Cash ($)	Stock Awards ($)	Option Awards ($)(1)	Non-Equity Incentive Plan Compen- sation ($)	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compen- sation ($)	Total ($)
Thomas D. Sullivan(2)							
Jeffrey W. Griffiths(2)							
Richard D. Tadler							
Martin F. Roper	$ 11,250		$ 12,335				$ 23,585
Douglas T. Moore	$ 11,250		$ 12,335				$ 23,585
John M. Presley	$ 11,250		$ 12,335				$ 23,585

(1) These options were granted under our 2006 Equity Plan for Non-Employee Directors and vest 25% on each of the first four anniversaries of grant, subject to acceleration in certain circumstances. The options have a strike price of $7.58 per share and expire July 13, 2016. Figures shown represent the dollar amounts of compensation cost recognized by us in 2006, in accordance with SFAS 123 (R), of director stock options. For a discussion of the assumptions relating to these valuations, see Summary of Significant Accounting Policies Stock-Based Compensation in Note 1 to our financial statements.

(2) We paid compensation to Messrs. Sullivan and Griffiths in their capacities as executive officers as detailed below.

2006 Equity Plan for Non-Employee Directors

Our 2006 Equity Plan for Non-Employee Directors, as amended effective October 18, 2006, provides for the grant of non-qualified stock options and restricted and unrestricted stock awards to non-employee directors. 200,000 shares are reserved for issuance under the plan, subject to adjustment to reflect changes in our stock due to corporate events such as reorganization, recapitalization, stock dividends, stock splits and reverse stock splits. The plan is administered by the board or a committee of the board composed of at least two directors (the 2006 Plan Committee). Fair market value is determined by the 2006 Plan Committee unless the stock is traded on a national securities exchange or automated quotation system, in which case the fair market value on any day will be the closing price reported on that day (except that on the first day on which the trading prices are so reported, the fair market value will be the price to the public stated in the final prospectus relating to our initial public offering). Options and restricted stock granted under the plan are non-transferable. At the request of a grantee and with the consent of the 2006 Plan Committee, grantees may receive a portion of cash compensation otherwise due to them in the form of unrestricted stock awards under the plan.

In the event of a 2006 Plan Sale Event (which includes our liquidation or dissolution, merger, sale of all or substantially all of our assets or a majority of our stock to an unrelated person, or any other transaction that results in a change ownership of a majority of voting control of us), the plan and all outstanding options terminate unless the parties to the transaction arrange to assume or continue the options following completion of the transaction. In the event of such a termination, holders will be given a specified period of time before the transaction to exercise outstanding options that are then exercisable or will become exercisable as of the effective time of the 2006 Plan Sale Event (subject to consummation of such 2006 Plan Sale Event). The board may amend or terminate the plan at any time, and the 2006 Plan Committee may amend or cancel any outstanding award, provided such action does not adversely affect the rights of the holder of any outstanding award without his or her consent.

Option grant agreements issued under the plan generally provide that options vest in four equal installments on the first four anniversaries of the applicable grant date, provided that (a) upon the occurrence of an initial public offering, vesting of the option will be accelerated by one year and (b) upon

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the occurrence of a 2006 Plan Sale Event, (i) 50% of the unvested portion of the option will vest and (ii) if the option is assumed or continued by us or any successor of us, the option will vest in full upon a termination of the optionee s service as a director within 18 months of such 2006 Plan Sale Event. Following a termination of the optionee s service as a director, the agreements generally provide that the option will remain exercisable (to the extent vested) for 12 months (in the case of the optionee s death or disability) or 90 days (in the case of termination of service as a director for any other reason). Shares acquired upon exercise of the option may be transferred only upon the optionee s death to his or her representatives, or to or for the benefit of certain family members, provided that we have a right of first refusal to purchase the shares prior to any such transfer. We also have the right to repurchase shares acquired through exercise of the option upon any termination of the optionee s service as a director or upon the optionee s bankruptcy, and have drag along rights in the event of certain events constituting a change in control of us. The transfer restrictions and drag along rights under the agreements terminate upon the occurrence of an initial public offering or 2006 Plan Sale Event.

2007 Plan

We expect to make future grants of stock options, restricted and unrestricted stock awards and other equity-based compensation to non-employee directors under our 2007 Plan. See Lumber Liquidators, Inc. 2007 Equity Compensation Plan below.

Compensation Discussion and Analysis

Our overall compensation philosophy is to maintain effective compensation programs that are as simple and flexible as possible, and permit us to make responsive adjustments to changing market conditions. We strive to provide our executive officers with compensation that is competitive within the industry and the executives geographic location in order to successfully attract and retain the key employees necessary to achieve the continued success of our business, being mindful of our desire to maintain low operating margins and control costs.

Prior to 2006, our founder and chairman of our board of directors (formerly our president and chief executive officer), Tom Sullivan, was responsible for making all non-equity based compensation decisions. Equity grants were not a regular part of our compensation program and very few equity grants had ever been made. In 2006, before Mr. Griffiths began serving as our chief executive officer, Mr. Sullivan continued to make all non-equity based compensation decisions, except for decisions regarding our annual bonus program, which were made in consultation with the board. Currently, Mr. Griffiths makes all non-equity based compensation decisions, subject to board oversight for annual bonus determinations. Equity grants are made by the board. As soon as practicable after the consummation of this offering, the compensation committee of our board of directors will assume responsibility for implementing and administering all aspects of our compensation and benefit plans and programs. We intend to have a compensation committee comprised solely of independent directors no later than the conclusion of the phase-in period required by the New York Stock Exchange for companies that are listing their shares in connection with an initial public offering.

Prior to 2004, our senior management consisted of Mr. Sullivan and a small team of executives at our Toano headquarters. In 2004, we began hiring additional members of senior management to manage our growth and strengthen our infrastructure with a view toward preparing for and consummating this offering, including the hiring or a new chief executive officer, a new chief information officer, a new vice president of operations and senior vice presidents of merchandising and direct marketing and advertising, during 2006 and 2007. By the end of 2006, we had significantly increased our senior management team at our Toano headquarters. As part of their respective compensation package, most of these new executives were granted stock options, which were intended to incentivize them to help achieve the successful completion of this offering and to strive to ensure our continued growth and success both before and after this offering.

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Following consummation of this offering, under the leadership of our compensation committee, we will continue to manage our compensation system with the following goals:

- to maintain a straightforward and flexible program that allows us to make adjustments in response to changes in market conditions;
- to provide compensation packages necessary to attract and retain key executives to help ensure that we remain competitive;
- to provide non-equity incentive compensation that depends on the executive s individual performance, and our financial performance, as compared against goals established by the compensation committee; and
- to provide an appropriate link between compensation and the creation of shareholder value through equity awards tied to our long-term performance.

Based on our overall compensation philosophy, our compensation program for senior management currently consists of only four basic elements to further and balance these goals:

- ***Base Salary.*** Existing compensation arrangements were negotiated with executives when they joined the company and, accordingly, we believe they reflect the compensation levels that were necessary to attract these executives. We intend to engage in benchmarking studies in the future to ensure that base salary levels remain competitive. We have not yet selected peer companies for these benchmarking purposes, although we currently expect to select peer companies from among those retail companies that have annual sales ranging from $150.0 million to $1.0 billion, with three- and five-year sales compound annual growth rates of at least 10%, but generally excluding those that are predominantly Internet- or catalog-based. In keeping with the theories underlying our commission-based compensation system for regional and store managers, our compensation for senior executives will continue to include performance-based compensation elements discussed below.
- ***Annual Cash Bonus Awards.*** Under our Annual Bonus Plan for Executive Management (the Bonus Plan), our senior executives are eligible to receive an annual incentive bonus awarded in cash. Bonuses will be tied to each executive s individual performance and our achievement of objective earnings thresholds, in each case as specifically tailored each year to reflect our then-current goals.
- ***Equity Incentive Awards.*** The long-term component of our compensation program consists of the grant of equity awards under our 2004 Stock Option and Grant Plan (the Option Plan), which are intended to create a mutuality of interest with shareholders by motivating our executive officers to manage our business so that our shareholders investment will grow in value over time.
- ***Performance-Based Commissions.*** Certain of our executives whose responsibilities relate directly to our sales are also eligible to receive commissions based on the sales levels we achieve.

We believe this system closely aligns our senior executives compensation with each executive s individual performance and with our performance on both a short-term and long-term basis and should assist us in attracting and retaining high-performing executives who will help us achieve continued success.

Base Salary. We are in the process of implementing annual performance reviews for senior management. Our president and chief executive officer, Jeffrey Griffiths, will conduct annual performance reviews of members of senior management, and our board will conduct annual evaluations of the chief executive officer s performance, in each case based on quantitative performance criteria such as sales, profitability and new account activity, and qualitative criteria such as business decisions, product and process suggestions and identification and development of business opportunities.

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Annual Cash Bonus Awards. Under the Bonus Plan, each executive officer is eligible to receive an annual cash bonus in an amount equal to a certain percentage of his or her base salary, based upon achievement of performance targets as set by the board of directors at the beginning of each calendar year. For calendar year 2006, performance targets for bonuses were based 50% on specified objective earnings thresholds for our audited earnings before income taxes, cash bonuses and non-cash stock compensation and 50% on a subjective analysis of individual operational goals established and/or approved by the chief executive officer (except for the chief executive officer, for whom the weighting was determined in the board s discretion).

The performance thresholds for the objective earnings component of our 2006 annual bonus plan were set in May 2006. This was the first time we set performance thresholds based on significant income statement or balance sheet line items, and it was done at a time when our budgeting process was still undergoing development. We believe that these objectives, as originally set, were aggressive and difficult to achieve. Shortly after the objectives were set, we made a number of changes to our operations, predominantly in connection with our transitioning toward becoming a public company, which made these objectives substantially more difficult to achieve. As a result, the original 2006 objectives do not reflect our current strategy or business model and are therefore not an appropriate benchmark against which to measure our past or future performance.

Our 2006 performance thresholds were as follows:

2006 Award Schedule Earnings Thresholds	% of Objective Portion of Bonus Earned
Up to $33,000,000	0
$33,000,000 or above	20%
$34,000,000 or above	40%
$35,700,000 or above	60%
$38,000,000 or above	70%
$39,000,000 or above	90%
$40,000,000 or above	100%

We did not have a specific bonus target for 2006. Our actual earnings (as calculated for purposes of making this determination) were below the minimum performance threshold, which we believe was principally due to the changes we made in our operations. Those changes, which included assembling an experienced executive team (including hiring a new chief executive officer), expanding our management team by hiring a number of senior vice presidents and a general counsel, restructuring our regional operations and increasing the number of regional managers, caused us to incur additional SG&A and other expenses during the period that had not been factored into our results in determining the objective performance thresholds. We also slowed the pace of new store openings to focus on expanding our store support infrastructure. See Management s Discussion and Analysis of Financial Condition and Results of Operations Overview.

Following are the target bonus amounts and actual bonus awards paid to each of these executive officers. We did not pay any portion of the bonus based on achievement of the objective earnings thresholds. The full amount of the bonus paid to each of these executive officers in 2006 was based solely upon satisfaction of the subjective individual operational goal criteria.

Executive	2006 Target Annual Bonus Amount	2006 Actual Annual Bonus Award
Mr. Sullivan	$ 300,000	$ 150,000
Mr. Griffiths	$ 142,466	$ 71,233
Mr. Terrell	$ 67,500	$ 33,750
Mr. Morrison	$ 206,250	$ 51,563
Mr. Pescara	$ 112,500	$ 42,188
Mr. Marcus	$ 62,500	$ 23,438
Mr. Greenan		

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In the future, our compensation committee will be responsible for establishing target bonus amounts and performance goals for executive bonuses. Factors to be considered may include, among other things, both quantitative performance criteria such as sales, profitability and new account activity, as well as qualitative criteria such as business decisions, product and process suggestions and identification and development of new business opportunities. While our board of directors is in the process of establishing 2007 bonus targets, no final determination has yet been made with respect to them.

Equity Incentive Awards. Our equity awards are designed to encourage executive officers to think and act like shareholders. We want our executive officers to take appropriate risks in order to generate returns for our shareholders and share in any adverse consequences if those risks cause poor performance or operating losses. The equity awards also reward longevity and increase retention, as we do not maintain a defined benefit pension plan or provide other post-retirement medical or life benefits. Because no benefit is received unless our stock price performs favorably over the term of the equity incentive award, such awards are intended to provide incentives for executive officers to enhance our long-term performance, as reflected in stock price appreciation over the long term, thereby increasing shareholder value. Prior to the consummation of this offering, the only equity awards granted to our executives are stock options that were awarded at the time the executives were hired. Future equity awards under the Option Plan may be in the form of stock options, restricted stock or unrestricted stock, as our compensation committee determines in its discretion.

As a private company, we limited the number of times per year that we granted options to our employees (including our executives) and prepared a valuation of our common stock in connection with each grant. Our compensation committee will determine our practices for granting future equity awards to our executive officers and other employees following the consummation of this offering.

We intend to implement new equity compensation plans in connection with the completion of this offering.

Performance-Based Commissions. We may continue to provide executives whose responsibilities relate directly to our sales with the opportunity to earn commissions based on the sales performance of their respective areas of responsibility. However, as more fully described below, Mr. Greenan is no longer eligible to receive commission payments.

Internal Pay Equity. As described above, annual bonuses represent a significant portion of annual compensation for our executive officers. The target bonus for each executive officer is based on a percentage of his base salary. For our named executive officers who participated in the annual bonus program in 2006, target bonus percentages ranged from 100% of base salary for our current chief executive officer and former chief executive officer, Mr. Griffiths and Mr. Sullivan, respectively, to 50% of base salary for Messrs. Terrell, Pescara and Marcus, as discussed more fully below.

Half of each executive officer s annual bonus is based on the achievement by the company of objective performance targets. Accordingly, the level of achievement by the company will be the same for each of our executive officers, and will have the same impact on bonus compensation for all of our executive officers. The other half of the annual bonuses are linked to a subjective assessment of each executive s individual performance. In 2006, this assessment was performed by the board with respect to Messrs. Griffiths and Sullivan, and was performed by Messrs. Griffiths and Sullivan and approved by the board with respect to each of our other named executive officers. In the future, we intend to continue having the board or compensation committee approve annual bonus amounts payable to a select group of our top executive officers. We believe that basing a portion of the bonuses on achievement of

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company-wide performance targets incentivizes all of our executives to work together in the interests of promoting shareholder value. We also believe it is appropriate to base a portion of each named executive officer s bonus on that person s individual performance. As a result of the structure of our bonus program, a material portion of our executive compensation may vary significantly from individual to individual and from year to year.

Mr. Griffiths 2006 annual bonus target was 100% of his base salary. This bonus percentage was the result of negotiations between us and Mr. Griffiths at the time he commenced employment with us. His annual bonus, granted in accordance with the annual bonus program described above, was prorated based on the portion of the 2006 calendar year during which he served as chief executive officer. Mr. Griffiths 2006 compensation also included a one-time signing bonus of $100,000, as well as a commitment to propose a 745,000 option grant to Mr. Griffiths at the next meeting of the board, both of which he received pursuant to his employment agreement in September. The one-time signing bonus was intended to attract Mr. Griffiths to accept employment at Lumber Liquidators. The equity grant was intended to provide him with a significant stake in our long-term future performance as we prepared to launch this offering.

2006 annual bonus targets for our other executive officers were as follows: Mr. Sullivan, 100%; Mr. Terrell, 50%; Mr. Morrison, 75%; Mr. Pescara, 50% and Mr. Marcus, 50%. In light of Mr. Greenan s opportunity to earn a significant performance-based commission for 2006, as more fully described below, he was not eligible to participate in the 2006 annual bonus program. We believe that these target payment levels provide significant and appropriate incentives for each of these executive officers.

In addition, during fiscal year 2006, Mr. Greenan functioned to a significant extent as a regional manager and, as a result, we felt it was appropriate for his compensation to mirror the compensation of the regional store managers. As a result, he received commission payments based on store operations. As Mr. Greenan has transitioned to a more centralized managerial role, his overall compensation package more closely resembles the packages of the other executive officers and he is no longer eligible to receive commission payments. Similarly, Mr. Pescara participated in a commission program in 2006, and the commission payments comprised a portion of his compensation. Mr. Pescara will continue to participate in a commission arrangement as a result of his direct responsibility for sales.

Equity awards for 2006 were approved by the board. The number of options awarded to each of our named executive officers in 2006 (listed in the Summary Compensation Table below) was determined based on the executive s position in us and the length of his service to us.

Policy on Code Section 162(m). As a private company, prior to the consummation of this offering we were not subject to the limits on deductibility of compensation set forth in Section 162(m) of the Internal Revenue Code. Section 162(m) denies publicly-held companies a tax deduction for annual compensation in excess of $1.0 million paid to their chief executive officer or any of their four other most highly compensated executive officers employed on the last day of a given year, unless their compensation is based on qualified performance criteria. Subject to certain transition rules that apply to companies that first become publicly held in connection with an initial public offering such as this offering, to qualify for deductibility, these criteria must be established by a committee of independent directors and approved, as to their material terms, by that company s stockholders. In future years, we intend to structure our bonus and equity incentive programs so that they qualify as performance-based compensation under Section 162(m). However, our compensation committee may approve compensation or changes to plans, programs or awards that may cause the compensation or awards not to comply with Section 162(m) if it determines that such action is appropriate and in our best interests.

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Executive Compensation

Summary Compensation Table

The following table presents certain summary information concerning compensation paid to or earned by our president and chief executive officer, our former president and chief executive officer, our chief financial officer, our former chief financial officer and, each of our three other most highly compensated executive officers (determined as of the end of the last fiscal year) whose total annual salary and bonus exceeded $100,000 during the fiscal year ended December 31, 2006 (together referred to herein as Named Executive Officers).

Name and Principal Position	Year	Salary ($)	Bonus ($)	Option Awards ($)(1)	Non-Stock Incentive Plan Compensation ($)	All Other Compensation ($)	Total ($)
Thomas D. Sullivan Former president and chief executive officer; Chairman of our board of directors(2)	2006	299,091	150,000			9,205	458,296
Jeffrey W. Griffiths President and chief executive officer(3)	2006	144,230	171,233	174,609			490,072
Daniel E. Terrell Chief financial officer(4)	2006	134,750	33,750	53,651		2,605	224,756
Robert M. Morrison Senior vice president, store operations(5)	2006	274,055	51,563	53,651		5,298	384,567
Marco Q. Pescara Senior vice president, direct marketing and advertising(6)	2006	156,351	42,188	18,502	18,494	35,769	271,304
H. Franklin Marcus, Jr. Former chief financial officer; Vice president, finance; Treasurer(7)	2006	122,720	23,438	53,651		9,457	209,266
Tyler Greenan Vice president, store operations(8)	2006	47,730		160,952	282,952	12,799	504,433

(1) Represents the dollar amount of compensation cost recognized by us in 2006, in accordance with SFAS 123 (R), of employee stock options. For a discussion of the assumptions relating to these valuations, see Summary of Significant Accounting Policies Stock-Based Compensation in Note 1 to our financial statements.

(2) Mr. Sullivan stepped down as our president and chief executive officer effective September 18, 2006. He continues to serve as chairman of our board of directors. Compensation shown for Mr. Sullivan represents compensation for his services as president and chief executive officer. He did not receive compensation in 2006 for his services as a director. Mr. Sullivan remains employed by the company, and will continue to receive compensation in that capacity. All other compensation includes $2,605 in group health plan contributions and life insurance premiums and $6,600 in matching contributions to our 401(k) plan.

(3) Mr. Griffiths was hired to serve as our chief executive officer as of September 18, 2006.

(4) Mr. Terrell became our chief financial officer effective October 2006. All other compensation includes $2,605 in group health plan contributions and life insurance premiums.

(5) Mr. Morrison was hired to serve as our senior vice president, store operations as of January 2, 2006. All other compensation includes $5,298 in group health plan contributions and life insurance premiums.

(6)

Mr. Pescara was hired to serve as our senior vice president, direct marketing and advertising as of April 20, 2006. The $18,494 represents a commission earned by Mr. Pescara. All other compensation includes reimbursement for $32,491 in relocation expenses and $3,278 in group health plan contributions and life insurance premiums.

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(7) Mr. Marcus stepped down as our chief financial officer effective October 2006. All other compensation includes $5,317 in group health plan contributions and life insurance premiums and $4,140 in matching contributions to our 401(k) plan.

(8) Non-Stock Incentive Plan Compensation represents a commission earned by Mr. Greenan. All other compensation includes $7,684 in group health plan contributions and life insurance premiums and $5,115 in matching contributions to our 401(k) plan.

Grants of Plan-Based Awards

The following table sets forth, for each of our Named Executive Officers, the grants of awards under any plan during the fiscal year ended December 31, 2006.

		Estimated Future Payouts Under Non-Equity Incentive Plan Awards ($)			Estimated Future Payouts Under Equity Incentive Plan Awards (#)			All Other Stock Awards: Number of Shares of Stock or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards ($/Sh)	Grant Date Fair Value of Equity Awards(1)
Name	**Grant Date**	**Threshold**	**Target**	**Max.**	**Threshold**	**Target**	**Max.**				
Thomas D. Sullivan											
Jeffrey W. Griffiths	10/18/06								745,000	7.83	2,793,750
Daniel E. Terrell	7/13/06								114,761	7.58	429,206
Robert M. Morrison	7/13/06								114,761	7.58	429,206
Marco Q. Pescara	7/13/06								39,577	7.58	148,022
H. Franklin Marcus, Jr.	7/13/06								114,761	7.58	429,206
Tyler C. Greenan	7/13/06								344,282	7.58	1,287,615

(1) For a discussion of the assumptions relating to these valuations, see Summary of Significant Accounting Policies Stock-Based Compensation in Note 1 to our financial statements.

Discussion of the Summary Compensation Table and Grants of Plan-Based Awards Table

Employment Agreement with Jeffrey W. Griffiths. Pursuant to the employment agreement entered into between us and Jeffrey W. Griffiths, Mr. Griffiths is employed as our president and chief executive officer for a four-year term commencing September 18, 2006. The agreement provides for an annual base salary of $500,000, which may be increased based on an annual performance review. In addition, our board of directors in its discretion may award Mr. Griffiths an annual performance bonus, based on our financial performance and Mr. Griffiths job performance, as described in more detail under Compensation Discussion and Analysis above. Under the agreement, Mr. Griffiths was granted options to purchase 745,000 shares of our stock (approximately 3% of our outstanding shares at that time) at fair market value as of October 18, 2006 (determined based on a valuation of the stock as of October 1, 2006). The options vest 25% on each of the first four anniversaries of grant, provided that the options will become fully vested upon the occurrence of a Griffiths Agreement Sale Event (defined as (i) our dissolution or liquidation, (ii) a sale of all or substantially all of our assets or (iii) a merger, reorganization or consolidation in which our stock is converted into or exchanged for securities of a successor entity and the holders of a majority of voting power prior to the transaction do not hold a majority of voting power of the successor entity following the transaction). Mr. Griffiths also received a $100,000 signing bonus under the agreement after the first thirty days of his employment (all or half of which he would have been required to return to us if his employment was terminated for cause or if he resigned without good reason (each as defined in his employment agreement) within the first six months, or after the first six months but within the first eighteen months, of his employment, respectively).

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The agreement also provides for certain payments in the event of termination, as described below under Potential Payments Upon Termination or Change of Control. Mr. Griffiths is bound under the agreement by a confidentiality provision, and non-competition and non-solicitation clauses that apply to his employment and for a period of two years following the later of the date of termination of Mr. Griffiths employment and the date (if any) that a court enters a judgment enforcing the relevant provision.

Employment Agreement with H. Franklin Marcus, Jr. On August 27, 2004, we entered into an employment agreement with H. Franklin Marcus, Jr., our treasurer and vice president, finance and former chief financial officer. Under the agreement, Mr. Marcus base salary for his first year of employment was $125,000, subject to annual review.

Employment Arrangement with Tyler C. Greenan. In 2006, we amended our compensation arrangement with Mr. Greenan, our vice president, store operations. Accordingly, his base salary is now $230,000. He is eligible for an annual bonus as discussed in more detail in Compensation Discussion and Analysis above.

Offer Letter Agreement with Robert M. Morrison. On December 28, 2005, we entered into an offer letter agreement with Robert M. Morrison, our senior vice president, store operations. Under the agreement, Mr. Morrison s base salary for his first year of employment was $275,000. He is eligible for an annual bonus as discussed in more detail in Compensation Discussion and Analysis above. At the time of hiring, Mr. Morrison received an initial option grant to purchase 114,760 shares of our stock and reimbursement for moving expenses (up to a maximum of $125,000). The agreement also provides for certain payments in the event of termination, as described below under Potential Payments Upon Termination or Change of Control.

Offer Letter Agreement with Marco Q. Pescara. On March 27, 2006, we entered into an offer letter agreement with Marco Pescara, our senior vice president, direct marketing and advertising. Under the agreement, Mr. Pescara s base salary for his first year of employment was $225,000. He is also entitled to receive a 0.25% monthly commission based on our e-commerce sales (subject to adjustment based on annual review) and an annual bonus as discussed in more detail in Compensation Discussion and Analysis above. At the time of hiring, Mr. Pescara received reimbursement for moving expenses and an initial stock option grant covering shares valued at $300,000 at the time of the grant (based on a third-party valuation of our stock), which vests over a three-year period, provided that (a) vesting shall accelerate by one year upon completion of an initial public offering, (b) the options will become fully vested in the event of a 2004 Plan Sale Event (as defined below under the description of our 2004 Stock Option and Grant Plan) or a reorganization, recapitalization, reclassification, stock dividend, stock split or similar change in our stock that lowers our overall value (in which case, Mr. Pescara would be included in any cash distribution in the same manner as a stockholder). The agreement also provides for certain payments in the event of termination, as described below under Potential Payments Upon Termination or Change of Control.

2004 Stock Option and Grant Plan. Our 2004 Stock Option and Grant Plan, as amended effective October 18, 2006, provides for the grant of incentive and non-qualified stock options and restricted and unrestricted stock awards to officers, employees, consultants and other key persons (including prospective employees). There are 2,100,000 shares reserved for issuance under the plan, subject to adjustment to reflect changes in our stock due to corporate events such as reorganization, recapitalization, stock dividends, stock splits and reverse stock splits. The plan is administered by the board or a committee of the board selected by the board (the 2004 Plan Committee), provided that the 2004 Plan Committee may delegate authority to the chief executive officer to grant awards (up to a specified quantity) at fair market value pursuant to guidelines established by the 2004 Plan Committee for determining the exercise price of options, the conversion ratio or price of other awards, and vesting criteria. The exercise price for

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options granted under the plan must be at least fair market value on the applicable grant date. Fair market value is determined by the 2004 Plan Committee unless the stock is traded on a national securities exchange or automated quotation system, in which case the fair market value on any day will be the closing price reported on that day (except that on the first day on which the trading prices are so reported, the fair market value will be the price to the public stated in the final prospectus relating to our initial public offering). Options and restricted stock granted under the plan are non-transferable. At the request of a grantee and with the consent of the 2004 Plan Committee, grantees may receive a portion of cash compensation otherwise due to them in the form of unrestricted stock awards under the plan.

In the event of a 2004 Plan Sale Event (which includes our liquidation or dissolution, merger, sale of all or substantially all of our assets or a majority of our stock to an unrelated person, or any other transaction that results in a change in ownership of a majority of voting control of us), the plan and all outstanding options terminate unless the parties to the transaction arrange to assume or continue the options following completion of the transaction. In the event of such a termination, holders will be given a specified period of time before the transaction to exercise outstanding options that are then exercisable or will become exercisable as of the effective time of the 2004 Plan Sale Event (subject to consummation of such 2004 Plan Sale Event). The board may amend or terminate the plan at any time, and the 2004 Plan Committee may amend or cancel any outstanding award, provided such action does not adversely affect the rights of the holder of any outstanding award without his or her consent.

Option grant agreements issued under the plan typically provide that options vest in four equal installments on the first four anniversaries of the applicable grant date, provided that (a) upon the occurrence of an initial public offering, vesting of the option will be accelerated by one year and (b) upon the occurrence of a 2004 Plan Sale Event, (i) 50% of the unvested portion of the option will vest and (ii) if the option is assumed or continued by us or any successor of us, the option will vest in full upon a termination of the optionee s employment without cause or by the optionee for good reason (in each case, as defined in the option grant agreements) within 18 months following the 2004 Plan Sale Event. Following a termination of the optionee s employment, the agreements generally provide that the option will remain exercisable (to the extent vested) for 12 months (in the case of the optionee s death or disability) or 90 days (in the case of termination of employment for any other reason). Options terminate immediately upon a termination of the optionee s employment for cause. Shares acquired upon exercise of the option may be transferred only upon the optionee s death to his or her representatives, or to or for the benefit of certain family members, provided that we have a right of first refusal to purchase the shares prior to any such transfer. We also have the right to repurchase shares acquired through exercise of the option upon any termination of the optionee s employment or upon the optionee s bankruptcy, and have drag along rights in the event of certain events constituting a change in control of us. The transfer restrictions and drag along rights under the agreements terminate upon the occurrence of an initial public offering or 2004 Plan Sale Event. Optionees are generally bound under the agreements by confidentiality, non-solicitation (of both customers and employees) and non-competition provisions during the optionee s employment and for a period of 12 months following termination of his or her employment, violation of which would result in forfeiture of all unexercised options (whether or not vested) and all shares acquired upon the exercise of options.

Lumber Liquidators, Inc. 2007 Equity Compensation Plan. In August 2007, our board of directors adopted, and our shareholders approved, the Lumber Liquidators, Inc. 2007 Equity Compensation Plan (the 2007 Plan). The 2007 Plan will be administered by our compensation committee or such other committee as our board of directors will appoint from time to time to administer and to otherwise exercise and perform the authority and functions assigned to such committee (the Committee).

The purpose of the 2007 Plan is to encourage and enable the employees, non-employee directors and other service providers of Lumber Liquidators and our related companies upon whose judgment, initiative and efforts we largely depend for the successful conduct of our business, to acquire a proprietary interest in

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the company. It is anticipated that providing these persons with a direct stake in our welfare will assure a closer identification of their interests with our interests, thereby stimulating their efforts on our behalf and strengthening their desire to remain with us.

The material terms of the 2007 Plan are summarized below. The summary is not a complete description of the terms of the 2007 Plan.

Eligible Participants and Types of Awards. The 2007 Plan provides for the grant of non-qualified and incentive stock options (Options) and other stock-based awards, including without limitation restricted stock, restricted stock units, unrestricted stock awards and stock appreciation rights (Options and other stock based awards are referred to herein as the Awards) to our employees, non-employee directors and other service providers. Awards may be settled in cash or in shares or other property pursuant to the terms of the relevant Award.

Shares Available for Awards and Individual Award Limits. The number of shares of our common stock authorized for issuance with respect to Awards granted under the 2007 Plan (Shares) is 4,300,000, reduced by (i) any Shares that have been issued under either the 2004 Stock Option and Grant Plan and the 2006 Equity Plan for Non-Employee Directors (collectively, the Prior Plans), and (ii) any Shares that are subject to outstanding awards under the Prior Plans that have not been forfeited or cancelled. Of those Shares, the maximum number of Shares that may be covered by incentive stock options within the meaning of Section 422 of the Internal Revenue Code of 1986 may not exceed 4,300,000. Shares issued under the 2007 Plan may be either newly issued shares or treasury shares. No more than 1,500,000 Shares may be issued as restricted stock (either as a separate award or to settle restricted stock units) or unrestricted stock.

The maximum number of Shares that may be covered by Incentive Awards granted under the 2007 Plan to any single participant (a participant) in any calendar year may not exceed 400,000 Shares.

Shares covered by Awards will only be counted as used to the extent they are actually issued and delivered to a participant (or a participant s permitted transferees). Accordingly, if an Award is settled for cash or if Shares are withheld to pay the exercise price of an Option or to satisfy any tax withholding requirement in connection with an Award, only the Shares issued (if any), net of the Shares withheld, will be deemed delivered for purposes of determining the number of Shares that remain available for delivery under the 2007 Plan. In addition, if Shares are issued subject to conditions which may result in the forfeiture, cancellation or return of such Shares to us, any portion of the Shares forfeited, cancelled or returned will be treated as not issued pursuant to the 2007 Plan. Furthermore, Shares owned by a participant (or a participant s permitted transferees) are tendered (either actually or through attestation) to us in payment of any obligation in connection with an Award, the number of Shares tendered will be added to the number of Shares that are available for delivery under the 2007 Plan.

Shares covered by Awards granted pursuant to the 2007 Plan in connection with the assumption, replacement, conversion or adjustment of outstanding equity-based awards in the context of a corporate acquisition or merger will not count as used under the 2007 Plan for these purposes.

Effect on Prior Plans. No further awards will be granted under any of the Prior Plans following this offering.

Administration. The Committee will from time to time designate those persons who will be granted Awards and the amount, type and other terms and conditions of such Awards. The Committee has full authority to administer the 2007 Plan, including authority to interpret and construe any provision of the 2007 Plan and the terms of any Award issued under it and to adopt such rules and regulations for administering the 2007 Plan, as it may deem necessary. Pursuant to this authority, on or after the date of

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grant of an Award under the 2007 Plan, the Committee may (i) accelerate the date on which any such Award becomes vested, exercisable or transferable, as the case may be; (ii) extend the term of any such Award, including, without limitation, extending the period following a termination of a participant s employment during which any such Award may remain outstanding; (iii) waive any conditions to the vesting, exercisability or transferability, as the case may be, of any such Award; or (iv) provide for the payment of dividends or dividend equivalents with respect to any such Award; provided that the Committee will not have any such authority to the extent that the grant of such authority would cause any tax to become due under Section 409A of the Internal Revenue Code.

Significant Features of Awards. The following is a description of the terms that apply to each Option issued under the 2007 Plan. Each Option will entitle the holder thereof to purchase a specified number of Shares. The exercise price of each Option will be at least equal to 100% of the fair market value of a Share on the date on which the Option is granted. Options will have terms that may not exceed ten years and will have vesting periods as determined by the Committee. Each Option will be exercisable in whole or in part, but no partial exercise of an Option will be for an aggregate exercise price of less than an amount determined by the Committee from time to time. Each agreement evidencing the award of each Option will specify the consequences with respect to such Option of the termination of the employment, service as a director or other relationship between us and the participant.

The Committee may also grant equity-based or equity-related Awards other than Options in such amounts and subject to such terms and conditions as the Committee determines. Each such Award may, among other things, (i) involve the transfer of actual Shares, either at the time of grant or thereafter, or payment in cash or otherwise of amounts based on the value of Shares; (ii) be subject to performance-based and/or service-based conditions; and (iii) be in the form of stock appreciation rights, phantom stock, restricted stock, restricted stock units, performance shares, deferred share units, share-denominated performance units or other full value stock awards. With respect to Awards of restricted stock or restricted stock units, the 2007 Plan specifies that vesting restrictions conditioned on employment and the passage of time may not expire less than three years from the date of grant (except that up to 100,000 Shares may be granted with a restriction of no less than one year), and restrictions conditioned on the achievement of performance goals or conditions may not expire less than one year from the date of grant. The Committee may, however, provide that restrictions will expire at any time as a result of the Disability, death or retirement of the 2007 Plan service provider or the occurrence of a change in control of the company.

Performance-Based Compensation. The Committee may grant Awards that are intended to qualify under the requirements of Section 162(m) of the Internal Revenue Code as performance-based compensation. The performance goals upon which the payment or vesting of any Award (other than Options) that is intended to so qualify depends may relate to one or more of the following performance measures: (i) pre-tax earnings, as shown in our annual report to shareholders, calculated in accordance with generally accepted accounting principles consistently applied by us; (ii) earnings per share, as shown in our annual report to shareholders, calculated in accordance with generally accepted accounting principles consistently applied by us; (iii) earnings before interest, taxes, depreciation and amortization calculated in accordance with generally accepted accounting principles consistently applied by us; (iv) sales; (v) market share; (vi) stock price; (vii) cash flow(s) (including operating or net cash flow(s)); (viii) financial return ratios; (ix) return measures, including return or net return on assets, net assets, equity, capital or gross sales; (x) adjusted pre-tax margin; (xi) operating margins, operating profits, and/or operating expenses; (xii) dividends; (xiii) net income or net operating income; (xiv) value of assets; (xv) market penetration with respect to specific designated products or product groups and/or specific geographic areas; (xvi) aggregate product price and other product measures; (xvii) expense or cost levels; (xviii) reduction of losses, loss ratios or expense ratios; (xix) reduction in fixed costs; (xx) operating cost management; (xxi) cost of capital; (xxii) debt reduction; (xxiii) productivity improvements; (xxiv) average inventory turnover; (xxv) satisfaction of specified business expansion goals or goals relating to

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acquisitions or divestitures; (xxvi) advertising efficiency; (xxvii) customer satisfaction based on specified objective goals or a company-sponsored customer survey; (xxviii) employee diversity goals or employee turnover; (xxix) supervision of litigation and information technology; and (xxx) goals relating to acquisitions or divestitures of subsidiaries or joint ventures. The targeted level or levels of performance with respect to such business criteria may be established at such levels and in such terms as the Committee may determine, in its discretion, including in absolute terms, on a per share basis (either basic or diluted), as a goal relative to performance in prior periods, or as a goal compared to the performance of one or more comparable companies or an index covering multiple companies.

Within 90 days after the beginning of a performance period, and in any case before 25% of the performance period has elapsed, we expect that the Committee will establish (i) performance goals and objectives for such performance period; (ii) target awards for each participant; and (iii) performance schedules or other objective methods for determining the applicable performance percentage to be applied to each such target award.

General Plan Provisions. The 2007 Plan provides for an adjustment in the number of Shares available to be issued under the 2007 Plan, the number of Shares subject to Awards and the exercise prices of certain Awards upon a change in our capitalization, a stock dividend or split, a merger or combination of Shares and certain other similar events.

The 2007 Plan also provides that participants may elect to satisfy certain federal income tax withholding requirements by remitting to us cash or, subject to certain conditions, Shares or by instructing us to withhold Shares payable to the participant.

Under the 2007 Plan, Awards may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner other than by will or by the laws of descent or distribution, except as permitted by the Committee on a general or specific basis.

Our board of directors may at any time suspend or discontinue the 2007 Plan or revise or amend it in any respect whatsoever, except that, no change shall be made that increases the total number of Shares reserved for Awards, materially modifies the requirements as to eligibility for participation in the 2007 Plan or materially increases the benefits accruing the participants in the 2007 Plan unless such change is approved by our shareholders, unless we or the Committee determines that no such shareholder approval is required under any applicable law, regulation or rule of a stock exchange applicable to the 2007 Plan.

We will not make any grants of Awards under the 2007 Plan following the tenth anniversary of the date that the 2007 Plan becomes effective.

The 2007 Plan provides for or permits accelerated vesting of certain types of Awards under certain circumstances in connection with a change in control of the company.

Tax Consequences of the 2007 Plan. The tax consequences of participation in the 2007 Plan for participants and us generally depend on the type of award issued to a participant. In general, if a participant recognizes ordinary income in connection with the grant, vesting or exercise of an award, we are entitled to a corresponding deduction equal to the amount recognized as income by the participant.

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Outstanding Equity Awards at Fiscal Year-End

The following table sets forth, for each of our Named Executive Officers, the outstanding equity awards as of the end of the fiscal year ended December 31, 2006.

	Option Awards					Stock Awards			
Name	**Number of Securities Underlying Unexercised Options (#) Exercisable**	**Number of Securities Underlying Unexercised Options (#) Unexercisable**	**Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#) (1)**	**Option Exercise Price ($)**	**Option Expiration Date**	**Number of Shares or Units of Stock That Have Not Vested (#)**	**Market Value of Shares or Units of Stock That Have Not Vested ($)**	**Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)**	**Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested ($)**
Thomas D. Sullivan									
Jeffrey W. Griffiths		745,000	745,000	7.83	10/18/2016				
Daniel E. Terrell		114,761	114,761	7.58	7/13/2016				
Robert M. Morrison		114,761	114,761	7.58	7/13/2016				
Marco Q. Pescara		39,577	39,577	7.58	7/13/2016				
H. Franklin Marcus, Jr.		114,761	114,761	7.58	7/13/2016				
Tyler C. Greenan		344,282	344,282	7.58	7/13/2016				

(1) Options shown were granted under our 2004 Stock Option and Grant Plan. The options held by each Named Executive Officer other than Mr. Pescara vest 25% on each of the first four anniversaries of grant. Mr. Pescara s options vest in three equal annual installments on the first three anniversaries of grant.

Option Exercises and Stock Vested

No Named Executive Officer exercised stock options, stock appreciation rights or similar instruments, and no equity-based awards vested, during the fiscal year ended December 31, 2006.

Potential Payments Upon Termination or Change of Control

Under his employment agreement, in the event of his disability or death, Mr. Griffiths is entitled to receive a prorated portion of his annual performance bonus. If (a) we terminate Mr. Griffiths employment without Cause (as defined in his agreement), (b) Mr. Griffiths terminates his employment within 60 days following a Griffiths Agreement Sale Event (as defined above under the description of Mr. Griffiths employment agreement) that results in a material reduction in his compensation or responsibilities or (c) Mr. Griffiths terminates his employment for Good Reason (as defined in his agreement), Mr. Griffiths is entitled to receive two times his base salary in either a lump sum or installments (at his election) and a prorated portion of his annual performance bonus. Upon the occurrence of a Griffiths Agreement Sale Event, Mr. Griffiths options will become fully vested.

Under his offer letter agreement, if Mr. Morrison is terminated without cause prior to December 28, 2007, he is entitled to receive severance equal to his annual salary.

Under Mr. Pescara s offer letter agreement, if he is terminated other than for cause (as defined in his agreement), he would be entitled to receive a severance payment equal to one year s base salary, projected commissions and bonus. If the termination occurs within 24 months following a sale of us, he would be entitled to receive 18 months base salary, projected commissions and bonus. In addition, the options granted to Mr. Pescara at the time he was hired (shown above in the Outstanding Equity Awards at Fiscal Year-End table) would become fully vested in the event of a 2004 Plan Sale Event (as defined above under the description of our 2004 Stock Option and Grant Plan) or a reorganization,

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recapitalization, reclassification, stock dividend, stock split or similar change in our stock that lowers our overall value (in which case, Mr. Pescara would be included in any cash distribution in the same manner as a stockholder).

Our other Named Executive Officers are not entitled to any severance payments upon termination of their employment or in connection with a change in control of us. If a change in control occurs, which constitutes a 2004 Plan Sale Event (as defined above under the description of our 2004 Stock Option and Grant Plan), the options held by our Named Executive Officers, as set forth in the Outstanding Equity Awards at Fiscal Year-End table above (other than options held by Mr. Griffiths and Mr. Pescara, which would vest pursuant to their respective employment and offer letter agreements as described above) would vest with respect to 50% of the unvested portion of the options. If such options were not assumed by us or a successor of us, the options would terminate upon the occurrence of a 2004 Plan Sale Event and optionees would be given a specified period of time prior to the transaction to exercise outstanding options that were then exercisable or (subject to consummation of the 2004 Plan Sale Event) that would become exercisable as of the effective time of the 2004 Plan Sale Event. If the options were assumed or continued by us or any successor of us, they would become fully vested if the optionee s employment were terminated without cause or by the optionee for good reason (in each case, as defined in the applicable stock option grant agreements) within 18 months following the 2004 Plan Sale Event. If a change in control that constituted a 2004 Plan Sale Event occurred as of December 31, 2006, the option spread for the options held by each of our Named Executive Officers would have been as follows: Mr. Griffiths, $1,341,000; Mr. Terrell, $117,630; Mr. Morrison, $117,630; Mr. Pescara, $81,133; Mr. Marcus, $117,630; Mr. Greenan, $352,889.

Other Agreements with Executive Officers

We have entered into employment agreements with Jeffrey W. Griffiths, H. Franklin Marcus, Jr., Robert M. Morrison and Marco Q. Pescara. For a summary of these agreements, see Executive Compensation Discussion of the Summary Compensation Table and Grants of Plan-Based Awards Table.

We have entered into employee confidentiality and non-compete agreements with certain of our executive officers, and we have entered into stock option agreements containing certain restrictive covenants with other of our executive officers, and we have entered into both agreements with two of our executive officers. Each employee confidentiality and non-compete agreement provides that the executive generally will not disclose, either during or after employment, our proprietary information, and will not compete with us or solicit our customers, suppliers or employees for the duration of the executive s employment and for a period of 24 months following termination of employment. The restrictive covenants of each stock option agreement provide that the executive generally will not disclose our proprietary information, compete with us or solicit our customers, suppliers or employees for the duration of the executive s employment and for a period of 12 months following termination of employment.

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CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS

Lease Arrangements

As of September 30, 2007, we leased our Toano facility, which includes a store location, and 23 of our other store locations from ANO LLC (ANO), a company that is wholly owned by Tom Sullivan, our founder and the chairman of our board of directors. We leased 22, 19 and 9 of our other stores from ANO as of December 31, 2006, 2005 and 2004, respectively. These leases generally have five-year base periods and multiple five-year renewal periods. We also lease our Toano finishing, distribution and headquarters facility from ANO under an operating lease with a base period that runs through December 31, 2019. Our rent expense attributable to ANO was $2.1 million, $2.0 million and $1.0 million in 2006, 2005 and 2004, respectively. Our future minimum lease payments to ANO under all of our leases with them were $18.2 million as of September 30, 2007. These leases are described in more detail in Note 6 to our audited financial statements included elsewhere in this prospectus.

As of September 30, 2007, we leased one store location each from DORA Real Estate Company, LLC (DORA), Wood on Wood Road, Inc. (Wood on Wood) and BMT Holdings, LLC (BMT). DORA and Wood on Wood are wholly owned by Tom, and he has a 50% membership interest in BMT. Each lease is for a five-year base period and has a five-year renewal period. The lease with BMT is currently in the first year of its renewal period. Our rent expense attributable to DORA was $0.02 million in each of 2006, 2005 and 2004. Our rent expense attributable to Wood on Wood was $0.07 million in each of 2006, 2005 and 2004. Our rent expense attributable to BMT was $0.05 million in each of 2006, 2005 and 2004.

We believe that the leases that we have signed to date with ANO, DORA, Wood on Wood and BMT are on fair market terms, and the stockholders agreement to which Tom and TA Associates are parties prevents entities affiliated with Tom from setting lease rates above market rates.

In addition, of our leases with lessors that are not owned in whole or in part by Tom, three were guaranteed by Tom as of September 30, 2007.

We have adopted new approval policies for related party transactions in connection with this offering. Pursuant to those policies, transactions between us and our directors, officers and employees are generally required to be approved by the disinterested members of the Board of Directors (or, once it has been formed, the audit committee). See Policy Concerning Related Party Transactions below.

Investment By TA Associates

In December 2004, we sold 7,952,018 shares of our series A convertible preferred stock for an aggregate amount of $35 million (the Preferred Stock Purchase) to TA IX L.P., TA/Atlantic and Pacific IV L.P., TA Strategic Partners Fund A L.P., TA Strategic Partners Fund B L.P. and TA Investors II L.P. (collectively, the TA Associates Funds). TA Associates, Inc. (TA Associates) is the ultimate general partner or manager of each of the TA Associates Funds, and Richard Tadler, one of our directors, is a managing director of TA Associates. After the Preferred Stock Purchase, TA Associates was the only holder of our series A convertible preferred stock. In connection with the closing of this offering, TA Associates will convert all of its shares of preferred stock into common stock based on a formula set forth in our restated articles of organization. The conversion ratio as of the date of this prospectus was one-to-one. Accordingly, TA Associates will receive 7,952,018 shares of common stock upon conversion of all the series A convertible preferred stock. TA Associates will sell 2,566,667 shares of common stock in this offering.

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Stockholders Agreement

In connection with the Preferred Stock Purchase, we entered into a stockholders agreement with Tom Sullivan and the TA Associates Funds relating to our shares of common stock, preferred stock and any other equity securities that we may issue and they may hold (collectively, the Agreement Shares). Among other things, the stockholders agreement places certain restrictions on the ability of Tom and the TA Associates Funds to transfer their Agreement Shares, gives rights of first refusal to the TA Associates Funds, Tom and, in certain circumstances, us, with respect to Agreement Shares sold by the TA Associates Funds or Tom and allows the TA Associates Funds, in certain circumstances, to sell their Agreement Shares in conjunction with a sale of Agreement Shares by Tom. In addition, the TA Associates Funds have preemptive rights in certain circumstances upon a sale by us of certain securities, including shares of our common stock. The stockholders agreement provides that we shall have five directors, one of whom shall be nominated by the TA Associates Funds and two of whom shall be nominated by Tom. The remaining two directors are independent, and both shall be nominated by Tom but must be deemed acceptable by the TA Associates Funds. Finally, among other things, we covenanted to furnish certain reports and financial statements to the TA Associates Funds, maintain certain insurance, permit certain inspections of our premises and obtain certain employee agreements. Except for certain covenants relating to liability insurance for directors and officers, compensation of directors and the provision of information to investors regarding certain tax matters, the provisions of the stockholders agreement relating to restrictions on transfer terminate upon the commencement of, and the remaining provisions of the stockholders agreement terminate upon the closing of, a Qualified Public Offering (as defined in our restated articles of organization). Although this offering is not expected to qualify as a Qualified Public Offering, we nonetheless expect to amend the stockholders agreement in connection with this offering.

Registration Rights Agreement

In connection with the Preferred Stock Purchase, we entered into a registration rights agreement with the TA Associates Funds relating to our shares of common stock held by the TA Associates Funds at any time. Subject to certain exceptions, including our right to defer a demand registration under certain circumstances, the TA Associates Funds have the right under the registration rights agreement to require us to register for public sale under the Securities Act all shares of common stock that they request be registered at any time following the expiration of the lock-up period in connection with this offering. After this offering, we are required to use our best efforts to qualify and remain qualified to register securities pursuant to a registration statement on Form S-3 under the Securities Act. The TA Associates Funds will also be entitled to piggyback registration rights with respect to any future registration statement we file for an underwritten public offering of securities. Under the registration rights agreement, we are responsible, subject to certain exceptions, for the expenses of any offering of the shares of the TA Associates Funds. The TA Associates Funds are subject to lock-up agreements for a period of 180 days following the date of this prospectus. The registration rights agreement does not include a liquidated damages clause and provides no penalty for liquidated damages.

Other Matters Involving Tom Sullivan

We are party to the Variable Plan, a stock-based agreement between Tom Sullivan and Kevin Sullivan, Tom s brother, who started our western U.S. operations and was our first regional manager, pursuant to which we generally guarantee Tom s cash payment obligation under the agreement. We account for that agreement as a variable performance plan. Under the Variable Plan, as amended in August 2005, Kevin has the right to a fixed ownership percentage of Lumber Liquidators, Inc. on a fully diluted basis, plus an additional ownership percentage based on certain performance criteria. The number of shares that may be acquired pursuant to the Variable Plan, shall be determined immediately prior to the completion of this offering, and will equal the sum of (a) a number of shares of common stock equal to 2.5% of our outstanding common stock, determined on a fully diluted basis and (b) a number of shares of common stock having an aggregate value equal to 10.5% of the value of the Western Region of the company. For purposes of the Variable Plan, the Western Region means our operations in eleven western U.S. states as of August 1, 2005, together with certain additional specified operations in those states, subject to adjustment in certain circumstances. The value of the Western Region will be determined by multiplying the fair market value of the company by a fraction, the numerator of which is the net income of the Western Region for the immediately preceding 12 months (or portion thereof) and the denominator of which is our net income for the same period, in each case determined in accordance with generally accepted accounting principles consistently applied. We estimate that the number of shares that would have been issued to Kevin pursuant to the Variable Plan had the option been exercised on September 30, 2007 would have been approximately 926,000 shares. This right is exercisable for shares of common stock, to be contributed by Tom and which have been placed in escrow, in conjunction with an IPO or sales event. Kevin s right under the Variable Plan will be considered to be exercised in full immediately prior to the completion of the initial public offering and, accordingly, we do not expect to record any future charges relating to the Variable Plan other than an adjustment in the quarter, in which this transaction closes to reflect the difference between the midpoint of the range shown on the cover page of this prospectus and the final closing price for the number of shares considered earned by Kevin. See Management s Discussion and Analysis of Financial Condition and Results of Operations Other Factors Affecting Our Results Equity Compensation Expenses.

The Variable Plan also contains various customary representations and warranties, put and call rights, termination provisions, certain lock-up provisions, and certain provisions that will terminate in connection with this offering, including a right of first refusal for Tom with respect to any disposal of the shares acquired by Kevin and a drag-along right in connection with various strategic transactions.

In 2004, we distributed cash of $42.6 million to Tom, of which $12.6 million consisted of cash distributions immediately prior to the TA Associates transaction, including $5.0 million to enable him to pay taxes on deemed income during the period when we were an S corporation, and a $30.0 million distribution related to the Preferred Stock Purchase. See Dividend Policy. In addition, pursuant to the terms of the Preferred Stock Purchase, Tom assumed a net liability related to a capitalized lease, and we recorded a $0.6 million contribution from him in 2005.

As of December 31, 2006, Tom owed us approximately $35,000 in connection with his personal use of our company s corporate credit card, which was paid in the first quarter of 2007. As of the date of this filing, Tom did not have an outstanding balance to us.

We expect to enter into arrangements to indemnify various parties, including Tom, against certain liabilities in connection with this offering, including liabilities under the Securities Act.

In August 2007, we conveyed two residential parcels of land unrelated to our business with a market land value assessed at less than $0.05 million in aggregate in Martin County, Florida to ANO to complete a transfer which Tom and TA Associates had intended to effect in connection with the December 2004 Preferred Stock Purchase. See Investment by TA Associates above.

Policy Concerning Related Party Transactions

In connection with this offering, we have adopted a formal written policy concerning related party transactions. A related party transaction is a transaction, arrangement or relationship involving us or a consolidated subsidiary (whether or not we or the subsidiary is a direct party to the transaction), on the one hand, and (i) a director, executive officer or employee of us or a consolidated subsidiary, his or her immediate family members or any entity that any of them controls or in which any of them has a substantial beneficial ownership interest; or (ii) any person who is the beneficial owner of more than 5% of our voting securities or a member of the immediate family of such person.

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The audit committee established prior to this offering (and, prior to that time, the disinterested members of the board of directors) evaluates each related party transaction for the purpose of recommending to the disinterested members of the board whether the transaction is fair, reasonable and within our company s policy, and should be ratified and approved by the board. At least annually, management will provide the audit committee or disinterested members of the board of directors, as the case may be, with information pertaining to related party transactions. Related party transactions entered into, but not approved or ratified as required by our policy concerning related party transactions, will be subject to termination by us or the relevant subsidiary, if so directed by the audit committee or the board, taking into account factors as such body deems appropriate and relevant.

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PRINCIPAL AND SELLING STOCKHOLDERS

The following tables set forth information known to us regarding beneficial ownership of our common stock as of October 20, 2007, by:

- each person, or group of affiliated persons, who beneficially owns more than 5% of our outstanding shares of common stock;
- each stockholder selling shares in this offering;
- each of our named executive officers;
- each of our directors; and
- all of our executive officers and directors as a group.

Except as otherwise set forth in the footnotes below, and subject to applicable community property laws, to our knowledge, each person has sole voting and investment power over the shares shown as beneficially owned. See Certain Relationships and Related Party Transactions for a discussion of business relationships between us and certain of our stockholders, and Management Executive Officers and Directors for the positions and offices held by certain stockholders.

The number of shares beneficially owned by each stockholder is determined under rules promulgated by the SEC and generally includes voting or investment power over the shares. The table below assumes the underwriters do not exercise their option to purchase additional shares. The information does not necessarily indicate beneficial ownership for any other purpose. Under SEC rules, for purposes of the calcuations in the table below, the number of shares of common stock deemed outstanding includes shares issuable upon exercise of options held by the respective person or group which may be exercised within 60 days after September 30, 2007. For purposes of calculating each person s or group s percentage ownership, shares of common stock issuable pursuant to stock options exercisable within 60 days after September 30, 2007 are included as outstanding and beneficially owned for that person or group, but are not treated as outstanding for the purpose of computing the percentage ownership of any other person or group.

As of October 20, 2007, there were 22,952,118 shares of our common stock outstanding (assuming the conversion into shares of common stock of all shares of our series A preferred stock currently held by the TA Associates Funds), excluding any shares issuable upon exercise of options. Assuming the completion of the various transactions described in this prospectus, there will be 26,752,118 shares of common stock outstanding upon completion of this offering, excluding any shares issuable upon exercise of options. Unless otherwise indicated in the footnotes, the address of each beneficial owner listed below is c/o Lumber Liquidators, Inc., 3000 John Deere Road, Toano, Virginia 23168.

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Beneficial Owner	Number of Shares Beneficially Owned Before the Offering	% of Outstanding Common Stock Before the Offering	Number of Shares of Common Stock Offered Hereby	Number of Shares Beneficially Owned After the Offering(1)	% of Outstanding Common Stock After the Offering(1)
TA Associates Funds(2)(3)	7,952,018	34.6%	2,566,667	5,385,351	20.1%
Thomas D. Sullivan(4)	15,000,100	65.4%	5,133,333	8,940,767	33.4%
Jeffrey W. Griffiths(5).	186,250	*	0	186,250	*
Douglas T. Moore(5)	13,193	*	0	13,193	*
John M. Presley(5)	13,193	*	0	13,193	*
Martin F. Roper(5)	13,193	*	0	13,193	*
Richard D. Tadler(6)	7,952,018	34.6%	2,566,667	5,385,351	20.1%
Daniel E. Terrell(5)	57,381	*	0	57,381	*
E. Livingston B. Haskell(5)	10,000	*	0	10,000	*
Rick A. Boucher	0	*	0	0	*
Robert M. Morrison(5)	57,381	*	0	57,381	*
Marco Q. Pescara(5)	26,385	*	0	26,385	*
Andrew P. Shulklapper	0	*	0	0	*
Kenneth M. Strohschein(5)	6,596	*	0	6,596	*
H. Franklin Marcus, Jr.(5)	57,381	*	0	57,381	*
Tyler C. Greenan(5)	172,141	*	0	172,141	*
All executive officers and directors as a group (15 persons)	23,565,212	100.0%	7,700,000	14,939,212	54.6%

* Represents beneficial ownership of less than 1%.

(1) Assumes no exercise of the underwriters option to purchase additional shares. In the event that option is exercised in full, TA Associates Funds and Richard Tadler would each beneficially own 4,810,351 shares of common stock, representing 18.0% of the outstanding common stock after the offering, and Tom Sullivan would beneficially own 7,790,767 shares of common stock, representing 29.1% of the outstanding common stock after the offering. In such a case, the percentage of the deemed outstanding shares of common stock beneficially owned by our directors and officers as a group after the offering would be 48.3%.

(2) Represents shares held by TA IX L.P., TA/Atlantic and Pacific IV L.P., TA Strategic Partners Fund A L.P., TA Strategic Partners Fund B L.P. and TA Investors II L.P. (the TA Associates Funds) TA Associates, Inc. is the ultimate general partner or manager of each of such entity. Investment and voting control of the TA Associates Funds is held by TA Associates, Inc. No stockholder, director or officer of TA Associates, Inc. has voting or investment power with respect to our shares of common stock held by the TA Associates Funds. Voting and investment power with respect to such shares is vested in a four-person investment committee consisting of the following employees of TA Associates, Inc.: Jonathan M. Goldstein, A. Bruce Johnston, C. Kevin Landry and Richard D. Tadler. The address of each TA Associates Fund and of TA Associates, Inc. is John Hancock Tower, 56th Floor, 200 Clarendon Street, Boston, Massachusetts 02116.

(3) The number of shares of common stock attributed to the TA Associates Funds gives effect to the conversion of each share of series A preferred stock currently held by the TA Associates Funds into shares of common stock in connection with this offering.

(4) With respect to shares owned after the offering, reflects the transfer of an estimated 926,000 shares from Mr. Sullivan to Kevin Sullivan pursuant to the Variable Plan as a result of the initial public offering.

(5) Consisting entirely of shares not currently owned but issuable upon the exercise of stock options awarded under our equity compensation plans that are currently exerciseable or become exerciseable within 60 days, including options that will vest as a result of the completion of this offering.

(6) Mr. Tadler is a managing director of TA Associates, Inc, which is the ultimate general partner or manager of each of the TA Associates Funds. Mr. Tadler may be deemed to be the beneficial owner of 7,952,018 shares of the post-conversion shares of common stock that will be held by the TA Associates Funds. Mr. Tadler disclaims beneficial ownership of any securities beneficially owned by the TA Associates Funds.

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DESCRIPTION OF CAPITAL STOCK

General

We were incorporated in Massachusetts in 1994, and, reincorporated in Delaware in August 2007 in connection with this offering. The following discussion is a summary of the terms of our capital stock, our certificate of incorporation and our bylaws following certain amendments that we intend to make in connection with this offering, as well as certain applicable provisions of Delaware law. Forms of our certificate of incorporation and bylaws as they will be in effect following this offering will be filed as exhibits to the registration statement of which this prospectus is a part.

Common Stock

Our authorized capital stock will consist of 35,000,000 shares of common stock, with a par value of $0.001 per share and 8,000,000 shares of preferred stock. Following the consummation of this offering, we will have 26,752,118 shares of common stock outstanding. Prior to this offering, there is one holder of our common stock and one holder of series A preferred stock that is convertible into our common stock.

Holders of common stock will be entitled to one vote for each share held on all matters submitted to a vote of stockholders and do not have cumulative voting rights. Accordingly, holders of a majority of the shares of common stock entitled to vote in any election of directors may elect all of the directors standing for election. In addition, holders of common stock are entitled to receive proportionately any dividends that may be declared by our board of directors, subject to any preferential dividend rights of outstanding preferred stock. Holders of common stock have no preemptive, subscription, redemption or conversion rights.

In the event of any reorganization of Lumber Liquidators with one or more corporations or a merger or share exchange of Lumber Liquidators with another corporation in which shares of our common stock are converted into or exchangeable for shares of stock, other securities or property, including cash, all holders of our common stock will be entitled to receive with respect to each share held the same kind and amount of shares of stock and other securities and property, including cash. Upon our liquidation, dissolution or winding up, the holders of common stock are entitled to receive proportionately our net assets available after the payment of all debts and other liabilities and subject to the prior rights of any outstanding preferred stock.

Our outstanding shares of common stock are, and the shares offered by us in this offering will be, when issued and paid for, validly issued, fully paid and nonassessable. The rights, preferences and privileges of holders of common stock are subject to, and may be impacted by, the rights of the holders of shares of any series of preferred stock that we may designate and issue in the future.

Preferred Stock

Our certificate of incorporation will authorize the issuance of an aggregate of 8,000,000 shares of preferred stock. Prior to the consummation of this offering, there were 7,952,018 shares of our series A preferred stock outstanding. We expect that all outstanding shares of series A preferred stock will be converted into common stock in connection with this offering. Upon the consummation of those transactions, there will be no shares of preferred stock outstanding.

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Our board of directors may, from time to time, direct the issue of shares of preferred stock in series and may, at the time of issue, determine the designation, powers, rights, preferences and limitations of each series. Satisfaction of any dividend preferences of outstanding preferred stock would reduce the amount of funds available for the payment of dividends on shares of common stock. Holders of preferred stock may be entitled to receive a preference payment in the event of any liquidation, dissolution or winding-up of Lumber Liquidators before any payment is made to the holders of common stock. Under certain circumstances, the issuance of preferred stock may render more difficult or tend to discourage a merger, tender offer or proxy contest, the assumption of control by a holder of a large block of securities of Lumber Liquidators or the removal of incumbent management. Upon the affirmative vote of a majority of the total number of directors then in office, the board of directors may issue shares of preferred stock with voting and conversion rights that could adversely affect the holders of shares of common stock.

Pre-emptive Rights

Our shareholders are not entitled to pre-emptive rights to subscribe for additional issuances of common stock or any other class or series of common stock or any security convertible into such stock.

Certain Certificate of Incorporation and Bylaw Provisions

Our certificate of incorporation will provide for the board to be divided into three classes, as nearly equal in number as possible, serving staggered terms. About one-third of the board will be elected annually, and each member will serve a three-year term. The provision for a classified board could prevent a party who acquires control of a majority of the outstanding voting shares from obtaining control of the board until the second annual shareholders meeting following the date the acquirer obtains the controlling share interest. The classified board provision is designed to have the effect of discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of Lumber Liquidators and to increase the likelihood that incumbent directors will retain their positions. Under Delaware law, directors of a corporation with a classified board may only be removed for cause unless the certificate of incorporation provides otherwise. Our certificate of incorporation does not provide that our shareholders can remove the directors without cause.

Our certificate of incorporation will provide that shareholder action can be taken only at an annual or special meeting of shareholders and cannot be taken by written consent in lieu of a meeting. Our bylaws provide that, except as otherwise required by law, annual or special meetings of the shareholders can only be called pursuant to a resolution adopted by a majority of the total number of directors then in office or by the chairman of the board. Shareholders are not permitted to call a general meeting or to require the board of directors to call a general meeting. The bylaws establish an advance notice procedure for shareholder proposals to be brought before a general meeting of shareholders, including proposed nominations of persons for election to the board of directors. Shareholders at a general meeting may only consider proposals or nominations specified in the notice of meeting or brought before the meeting by or at the direction of the board of directors or by a shareholder who was a shareholder of record on the record date for the meeting, who is entitled to vote at the meeting and who has given timely written notice, in proper form, of the shareholder s intention to bring that business before the meeting. Although neither the certificate of incorporation nor the bylaws gives the board of directors the power to approve or disapprove shareholder nominations of candidates or proposals about other business to be conducted at a general meeting, the certificate of incorporation and the bylaws may have the effect of precluding the conduct of certain business at a meeting if the proper procedures are not followed or may discourage or deter a potential acquirer from conducting a solicitation of proxies to elect its own slate of directors or otherwise attempting to obtain control of Lumber Liquidators.

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We expect the certificate of incorporation to provide that the provisions of Section 203 of the Delaware General Corporation Law, which relate to business combinations with interested shareholders, will apply to Lumber Liquidators. Section 203 provides that, subject to certain exceptions, an interested stockholder of a Delaware corporation may not engage in any business combination, including mergers or consolidations or acquisitions of additional shares of the corporation, with the corporation for a three-year period following the date that the stockholder becomes an interested stockholder. Under Section 203, an interested stockholder is a person who, together with affiliates and associates, owns or, in some cases, within three years prior owned, 15% or more of the corporation s voting stock.

Our board of directors will be permitted to alter certain provisions of our bylaws without obtaining shareholder approval.

Limitation of Liability and Indemnification of Officers and Directors

Our certificate of incorporation will provide that no director shall be liable to us or our stockholders for monetary damages for breach of fiduciary duty as a director, except as required by the Delaware General Corporation Law as in effect from time to time. Our bylaws will provide that, to the full extent permitted by law, we will indemnify any person made or threatened to be made a party to any action by reason of the fact that the person is or was our director or officer, or serves or served as a director or officer of any other enterprise at our request.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is Computershare Trust Company, N.A.

Listing

We will apply to list our common stock on the New York Stock Exchange under the symbol LL.

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SHARES ELIGIBLE FOR FUTURE SALE

Prior to this offering, there has been no public market for our common stock. Upon completion of this offering, we will have outstanding an aggregate of 26,752,118 shares of common stock, assuming no exercise of outstanding options. All of the shares sold in this offering will be freely tradable without restriction or further registration under the Securities Act, except that any shares purchased by our affiliates, as that term is defined in Rule 144, may generally only be sold in compliance with the limitations of Rule 144, which is summarized below. We are not aware of any of our affiliates who will acquire shares in this offering. On that basis, all of the remaining shares of our common stock that are outstanding upon completion of this offering, or 15,252,118 shares, will be restricted shares under the terms of the Securities Act and may be eligible for sale as described below 180 days after the date of the final prospectus following the expiration of lock-up agreements between our officers, directors and stockholders and the underwriters. Goldman, Sachs & Co. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, in their sole discretion, may release any of the securities subject to these lock-up agreements without notice at any time.

Sales of Restricted Securities

Restricted shares may be sold in the public market only if they are registered under the Securities Act or if they are sold pursuant to an exemption from registration, such as the exemptions provided by Rule 144, 144(k) or 701 promulgated under the Securities Act, each of which is summarized below.

In general, under Rule 144 as currently in effect, beginning 90 days after the date of this prospectus a person who has beneficially owned restricted shares for at least one year and has complied with the requirements described below would be entitled to sell within any three-month period a number of shares that does not exceed the greater of one percent of the number of shares of common stock then outstanding, which will equal approximately 267,521 shares immediately upon completion of this offering, or the average weekly trading volume of our common stock on the New York Stock Exchange during the four calendar weeks preceding the filing of a notice on Form 144 reporting the sale. Sales under Rule 144 are also restricted by manner of sale provisions, notice requirements and the availability of current public information about us. Rule 144 also provides that our affiliates who are selling shares of our common stock that are not restricted shares must comply with the same restrictions applicable to restricted shares with the exception of the one-year holding period requirement.

Under Rule 144(k), a person who is not deemed to have been our affiliate at any time during the three months preceding a sale, and who has beneficially owned the shares proposed to be sold for at least two years, including the holding period of any prior owner that is not an affiliate of ours, is entitled to sell those shares without complying with the manner of sale, public information, volume limitation or notice provisions of Rule 144. Accordingly, unless otherwise restricted, any such shares may be sold upon the expiration of the lock-up period described below.

Shares issued in reliance on Rule 701, such as the shares of common stock acquired upon the exercise of options or pursuant to other rights granted under our equity incentive plans, are also restricted, and may be resold, to the extent not restricted by the terms of the lock-up agreements by non-affiliates beginning 90 days after the date of this prospectus, subject only to the manner of sale provisions of Rule 144, and by affiliates under Rule 144, without compliance with its one-year minimum holding period. Of the total shares issuable upon exercise of options that have vested or will vest in the 180-day period following this offering, 715,472 are subject to 180-day lock-up agreements covering that period.

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Additional Registration Statements

Equity Incentive Plans

We intend to file one or more registration statements under the Securities Act after the offering to register up to 4.3 million shares of our common stock underlying outstanding stock options or reserved for issuance under our equity incentive plans. These registration statements will become effective upon filing, and shares covered by these registration statements will be eligible for sale in the public market immediately after the effective dates of these registration statements, subject to the lock-up agreements described below.

Effects of Sales of Shares

Prior to this offering, there has been no public market for shares of our common stock. We cannot predict what effect, if any, that sales of shares of our common stock from time to time, or the availability of shares of our common stock for future sale, may have on the price for shares of our common stock. Sales of substantial amounts of common stock, or the perception that such sales could occur, could adversely affect prevailing prices for our common stock and could impair our future ability to obtain capital through an offering of equity securities.

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UNDERWRITING

The company, the selling stockholders and the underwriters named below have entered into an underwriting agreement with respect to the shares being offered. Subject to certain conditions, each underwriter has severally agreed to purchase the number of shares indicated in the following table. Goldman, Sachs & Co. and Merrill Lynch, Pierce, Fenner & Smith Incorporated are the representatives of the underwriters.

Underwriters	**Number of Shares**
Goldman, Sachs & Co.	
Merrill Lynch, Pierce, Fenner & Smith Incorporated	
Lehman Brothers Inc.	
Banc of America Securities LLC	
Piper Jaffray & Co.	
Total	11,500,000

The underwriters are committed to take and pay for all of the shares being offered, if any are taken, other than the shares covered by the option described below unless and until this option is exercised.

If the underwriters sell more shares than the total number set forth in the table above, the underwriters have an option to buy up to an additional 1,725,000 shares from the selling stockholders to cover such sales. They may exercise that option for 30 days. If any shares are purchased pursuant to this option, the underwriters will severally purchase shares in approximately the same proportion as set forth in the table above.

The following tables show the per share and total underwriting discounts and commissions to be paid to the underwriters by the company and the selling shareholders. Such amounts are shown assuming both no exercise and full exercise of the underwriters option to purchase additional shares.

Paid by the Company	**No Exercise**	**Full Exercise**
Per Share	$	$
Total	$	$

Paid by the Selling Stockholders	**No Exercise**	**Full Exercise**
Per Share	$	$
Total	$	$

Shares sold by the underwriters to the public will initially be offered at the initial public offering price set forth on the cover of this prospectus. Any shares sold by the underwriters to securities dealers may be sold at a discount of up to $ per share from the initial public offering price. If all the shares are not sold at the initial public offering price, the representatives may change the offering price and the other selling terms.

The company and its officers, directors, and holders of substantially all of the company s common stock, including the selling stockholders, have agreed with the underwriters, subject to certain exceptions, not to dispose of or hedge any of their common stock or securities convertible into or exchangeable for shares of common stock during the period from the date of this prospectus continuing through the date 180 days after the date of this prospectus, except with the prior written consent of the representatives. This agreement does not apply to any existing employee benefit plans. See Shares Available for Future Sale for a discussion of certain transfer restrictions.

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The 180-day restricted period described in the preceding paragraph will be automatically extended if: (1) during the last 17 days of the 180-day restricted period the company issues an earnings release or announces material news or a material event; or (2) prior to the expiration of the 180-day restricted period, the company announces that it will release earnings results during the 15-day period following the last day of the 180-day period, in which case the restrictions described in the preceding paragraph will continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release or announcement of the material news or material event.

Prior to the offering, there has been no public market for the shares. The initial public offering price has been negotiated among the company and the representatives. Among the factors to be considered in determining the initial public offering price of the shares, in addition to prevailing market conditions, will be the company s historical performance, estimates of the business potential and earnings prospects of the company, an assessment of the company s management and the consideration of the above factors in relation to market valuation of companies in related businesses.

An application will be made to list the common stock on the New York Stock Exchange under the symbol LL. In order to meet one of the requirements for listing the common stock on the New York Stock Exchange, the underwriters have undertaken to sell lots of 100 or more shares to a minimum of 400 beneficial holders and thereby establish at least 1,100,000 shares in the public float having a minimum aggregate market value of $60 million.

In connection with the offering, the underwriters may purchase and sell shares of common stock in the open market. These transactions may include short sales, stabilizing transactions and purchases to cover positions created by short sales. Short sales involve the sale by the underwriters of a greater number of shares than they are required to purchase in the offering. Covered short sales are sales made in an amount not greater than the underwriters option to purchase additional shares from the selling stockholders in the offering. The underwriters may close out any covered short position by either exercising their option to purchase additional shares or purchasing shares in the open market. In determining the source of shares to close out the covered short position, the underwriters will consider, among other things, the price of shares available for purchase in the open market as compared to the price at which they may purchase additional shares pursuant to the option granted to them. Naked short sales are any sales in excess of such option. The underwriters must close out any naked short position by purchasing shares in the open market. A naked short position is more likely to be created if the underwriters are concerned that there may be downward pressure on the price of the common stock in the open market after pricing that could adversely affect investors who purchase in the offering. Stabilizing transactions consist of various bids for or purchases of common stock made by the underwriters in the open market prior to the completion of the offering.

The underwriters may also impose a penalty bid. This occurs when a particular underwriter repays to the underwriters a portion of the underwriting discount received by it because the representatives have repurchased shares sold by or for the account of such underwriter in stabilizing or short covering transactions.

Purchases to cover a short position and stabilizing transactions, as well as other purchases by the underwriters for their own accounts, may have the effect of preventing or retarding a decline in the market price of the company s stock, and together with the imposition of the penalty bid, may stabilize, maintain or otherwise affect the market price of the common stock. As a result, the price of the common stock may be higher than the price that otherwise might exist in the open market. If these activities are commenced, they may be discontinued at any time. These transactions may be effected on the New York Stock Exchange, in the over-the-counter market or otherwise.

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a Relevant Member State), each underwriter has represented and agreed

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that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the Relevant Implementation Date) it has not made and will not make an offer of shares to the public in that Relevant Member State prior to the publication of a prospectus in relation to the shares which has been approved by the competent authority in that Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, all in accordance with the Prospectus Directive, except that it may, with effect from and including the Relevant Implementation Date, make an offer of shares to the public in that Relevant Member State at any time:

(a) to legal entities which are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;

(b) to any legal entity which has two or more of (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than □43,000,000 and (3) an annual net turnover of more than □50,000,000, as shown in its last annual or consolidated accounts;

(c) to fewer than 100 natural or legal persons (other than qualified investors as defined in the Prospectus Directive) subject to obtaining the prior consent of the representatives for any such offer; or

(d) in any other circumstances which do not require the publication by the company of a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an offer of shares to the public in relation to any shares in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the shares to be offered so as to enable an investor to decide to purchase or subscribe the shares, as the same may be varied in that Relevant Member State by any measure implementing the Prospectus Directive in that Relevant Member State and the expression Prospectus Directive means Directive 2003/71/EC and includes any relevant implementing measure in each Relevant Member State.

Each underwriter has represented and agreed that:

(a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the Financial Services and Markets Act 2000 (the FSMA)) received by it in connection with the issue or sale of the shares in circumstances in which Section 21(1) of the FSMA would not, if the company was not an authorized person, apply to the company; and

(b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the shares in, from or otherwise involving the United Kingdom.

The shares may not be offered or sold by means of any document other than (i) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), or (ii) to professional investors within the meaning of the Securities and Futures Ordinance (Cap.571, Laws of Hong Kong) and any rules made thereunder or (iii) in other circumstances which do not result in the document being a prospectus within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), and no advertisement, invitation or document relating to the shares may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to shares which are or are intended to be disposed of only to persons outside Hong Kong or only to professional investors within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

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This prospectus has not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, this prospectus and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the shares may not be circulated or distributed, nor may the shares be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the SFA), (ii) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the shares are subscribed or purchased under Section 275 by a relevant person which is: (a) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries rights and interest in that trust shall not be transferable for 6 months after that corporation or that trust has acquired the shares under Section 275 except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; or (3) by operation of law.

The securities have not been and will not be registered under the Securities and Exchange Law of Japan (the Securities and Exchange Law) and each underwriter has agreed that it will not offer or sell any securities, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to a resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Securities and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

The underwriters do not expect sales to discretionary accounts to exceed five percent of the total number of shares offered.

The company and the selling stockholders estimate that their share of the total expenses of the offering, excluding underwriting discounts and commissions, will be approximately $2.5 million.

The company and the selling stockholders will agree to indemnify the several underwriters against certain liabilities, including liabilities under the Securities Act of 1933.

Certain of the underwriters and their respective affiliates have, from time to time, performed, and may in the future perform, various financial advisory and investment banking services for the company, for which they received or will receive customary fees and expenses. An affiliate of Banc of America Securities LLC is the lender under our new revolving credit agreement and the term-loan portion of our senior secured loan agreement.

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VALIDITY OF THE COMMON STOCK

The validity of the common stock offered hereby will be passed upon for us by Cleary Gottlieb Steen & Hamilton LLP, New York, New York, and for the underwriters by Sullivan & Cromwell LLP, New York, New York.

EXPERTS

The financial statements of Lumber Liquidators, Inc. at December 31, 2006 and 2005, and for each of the three years in the period ended December 31, 2006, appearing in this Prospectus and Registration Statement have been audited by Ernst & Young LLP, independent registered public accounting firm, as set forth in their report thereon appearing elsewhere herein, and are included in reliance upon such report given on the authority of such firm as experts in accounting and auditing.

WHERE YOU CAN FIND ADDITIONAL INFORMATION

We have filed with the SEC a registration statement on Form S-1 under the Securities Act of 1933 registering the common stock to be sold in this offering. As permitted by the rules and regulations of the SEC, this prospectus does not contain all of the information included in the registration statement and the exhibits and schedules filed as a part of the registration statement. For more information concerning us and the common stock to be sold in this offering, you should refer to the registration statement and to the exhibits and schedules filed as part of the registration statement.

The registration statement, including the exhibits and schedules filed as a part of the registration statement, may be inspected at the public reference room of the SEC at 100 F Street, N.E., Room 1580, Washington, DC 20549 and copies of all or any part thereof may be obtained from that office upon payment of the prescribed fees. You may call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference room and you can request copies of the documents upon payment of a duplicating fee, by writing to the SEC. In addition, the SEC maintains a website that contains reports, proxy and information statements and other information regarding registrants, including us, that file electronically with the SEC which can be accessed at http://www.sec.gov.

As a result of the filing of the registration statement, we will become subject to the information and reporting requirements of the Securities Exchange Act of 1934, and will file periodic proxy statements and will make available to our stockholders annual reports containing audited financial information for each year and quarterly reports for the first three quarters of each year containing unaudited interim financial information.

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Lumber Liquidators, Inc.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors

Lumber Liquidators, Inc.

We have audited the accompanying balance sheets of Lumber Liquidators, Inc. as of December 31, 2006 and 2005, and the related statements of income, stockholder s equity (deficit), and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company s internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lumber Liquidators, Inc. at December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the financial statements, effective January 1, 2006, Lumber Liquidators, Inc. adopted Financial Accounting Standards Board Statement No. 123(R), Share-Based Payment, applying the prospective-transition method.

/s/ Ernst & Young LLP

Richmond, Virginia

March 26, 2007

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Lumber Liquidators, Inc.

Balance Sheets

(in thousands, except share data)

	December 31, 2006	December 31, 2005
Assets		
Current Assets:		
Cash and Cash Equivalents	$ 3,965	$ 6,031
Merchandise Inventories	51,758	30,009
Prepaid Expenses	3,638	1,984
Other Current Assets	3,359	2,644
Total Current Assets	**62,720**	**40,668**
Property and Equipment, net	9,332	9,515
Deferred Income Taxes	3,737	2,819
Other Assets	2,231	2,160
Total Assets	**$ 78,020**	**$ 55,162**
Liabilities and Stockholder s Equity (Deficit)		
Current Liabilities:		
Accounts Payable	$ 16,296	$ 8,412
Customer Deposits and Store Credits	6,804	7,360
Accrued Compensation	1,566	1,041
Other Current Liabilities	5,292	3,928
Current Portion of Long-Term Debt	2,804	2,450
Current Portion of Capital Lease Obligations	261	418
Total Current Liabilities	**33,023**	**23,609**
Long-Term Debt	6,479	7,194
Capital Lease Obligations	59	298
Stock Compensation Liability	9,132	8,092
Redeemable Preferred Stock	34,795	34,744
Stockholder s Equity (Deficit):		
Common Stock (No par value; authorized: 35,000,000 and 24,500,000 shares at December 31, 2006 and 2005, respectively; issued and outstanding: 15,000,100 at December 31, 2006 and 2005)		
Additional Capital	1,250	841
Retained Earnings (Deficit)	(6,718)	(19,616)
Total Stockholder s Equity (Deficit)	**(5,468)**	**(18,775)**
Total Liabilities and Stockholder s Equity (Deficit)	**$ 78,020**	**$ 55,162**

See accompanying notes to financial statements

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Lumber Liquidators, Inc.

Statements of Income

(in thousands, except share data and per share amounts)

	Year Ended December 31, 2006	2005	2004
Net Sales	**$ 332,060**	**$ 244,947**	**$ 171,766**
Cost of Sales	221,931	158,844	115,857
Gross Profit	**110,129**	**86,103**	**55,909**
Operating Expenses:			
Selling, General and Administrative Expenses	88,716	67,900	48,461
Impairment Loss on Long-Lived Assets			293
Total Operating Expenses	**88,716**	**67,900**	**48,754**
Operating Income	**21,413**	**18,203**	**7,155**
Interest Expense	722	638	429
Other (Income) Expense	(368)	(96)	190
Income Before Income Taxes	**21,059**	**17,661**	**6,536**
Provision for Income Taxes	8,161	6,948	(1,450)
Net Income	**$ 12,898**	**$ 10,713**	**$ 7,986**
Net Income per Common Share Basic	**$ 0.86**	**$ 0.71**	**$ 0.53**
Net Income per Common Share Diluted	**$ 0.56**	**$ 0.46**	**$ 0.51**
Weighted Average Common Shares Outstanding:			
Basic	15,000,100	15,000,100	15,000,100
Diluted	22,989,403	23,063,174	15,675,477

See accompanying notes to financial statements

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Lumber Liquidators, Inc.

Statements of Stockholder s Equity (Deficit)

(in thousands, except share data)

	Common Stock			Retained	
	Shares	Par Value	Additional Capital	Earnings (Deficit)	Total Stockholder s Equity (Deficit)
Balance December 31, 2003	**100**	**$**	**$ 1**	**$ 3,619**	**$ 3,620**
Common Stock Dividend	15,000,000				
Distributions to Founder, net				(41,934)	(41,934)
Stock-Based Compensation Expense			86		86
Net Income				7,986	7,986
Balance December 31, 2004	**15,000,100**	**$**	**$ 87**	**$ (30,329)**	**$ (30,242)**
Contributions from Founder, net			581		581
Stock-Based Compensation Expense			173		173
Net Income				10,713	10,713
Balance December 31, 2005	**15,000,100**	**$**	**$ 841**	**$ (19,616)**	**$ (18,775)**
Stock-Based Compensation Expense			409		409
Net Income				12,898	12,898
Balance December 31, 2006	**15,000,100**	**$**	**$ 1,250**	**$ (6,718)**	**$ (5,468)**

See accompanying notes to financial statements

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Lumber Liquidators, Inc.

Statements of Cash Flows

(in thousands)

	Year Ended December 31,		
	2006	**2005**	**2004**
Cash Flows from Operating Activities:			
Net Income	$ 12,898	$ 10,713	$ 7,986
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Depreciation and Amortization	2,908	2,240	1,157
Deferred Income Taxes	(697)	(1,732)	(1,695)
Stock-Based Compensation Expense	1,449	3,306	3,024
Accretion of Redeemable Preferred Stock	51	51	
Impairment Loss on Long-Lived Assets			293
Changes in Operating Assets and Liabilities:			
Merchandise Inventories	(21,749)	(7,502)	(7,597)
Accounts Payable	7,884	(1,261)	2,308
Customer Deposits and Store Credits	(556)	2,245	1,387
Prepaid Expenses and Other Current Assets	(2,590)	(2,026)	(1,230)
Other Assets and Liabilities	1,812	1,954	499
Net Cash Provided by Operating Activities	**1,410**	**7,988**	**6,132**
Cash Flows from Investing Activities:			
Purchases of Property and Equipment	(2,719)	(4,327)	(6,547)
Purchase of Hardwood Holdings, LLC			(1,050)
Net Cash Used in Investing Activities	**(2,719)**	**(4,327)**	**(7,597)**
Cash Flows from Financing Activities:			
Proceeds from Long-Term Borrowings and Revolving Line	1,464	2,140	11,930
Repayments of Long-Term Debt	(1,825)	(3,009)	(1,609)
Principal Payments on Capital Lease Obligations	(396)	(500)	(979)
Proceeds from Sale of Redeemable Preferred Stock			35,000
Contributions from (Distributions to) Founder		708	(42,612)
Redeemable Preferred Stock Issuance Costs			(307)
Net Cash (Used In) Provided by Financing Activities	**(757)**	**(661)**	**1,423**
Net (Decrease) Increase in Cash and Cash Equivalents	(2,066)	3,000	(42)
Cash and Cash Equivalents, Beginning of Year	6,031	3,031	3,073
Cash and Cash Equivalents, End of Year	**$ 3,965**	**$ 6,031**	**$ 3,031**

See accompanying notes to financial statements

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Lumber Liquidators, Inc.

Notes to Financial Statements

(amounts in thousands, except share data and per share amounts)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
Nature of Business

Lumber Liquidators, Inc. (the Company) is a multi-channel specialty retailer of hardwood flooring, and hardwood flooring enhancements and accessories, operating as a single business segment. The Company offers an extensive assortment of exotic and domestic hardwood species, engineered hardwoods, and laminates direct to the consumer. The Company also features the renewable flooring products bamboo and cork, and provides a wide selection of flooring enhancements and accessories, including moldings, noise-reducing underlay and adhesives. These products are primarily sold under the Company s private label brands, including the premium Bellawood floors. The Company sells primarily to homeowners or to contractors on behalf of homeowners through a network of stores located in primary or secondary metropolitan areas throughout the United States. In addition to the store locations, the Company s products may be ordered, and customer questions/concerns addressed, through both our call center in Toano, Virginia, and our website, LumberLiquidators.com. The Company finishes the majority of the Bellawood products in Toano, Virginia, which along with the call center, corporate offices and distribution facility represent the Corporate Headquarters.

Organization and Basis of Financial Statement Presentation

The Company was organized in 1994 as a Massachusetts corporation. The original equity interest was held solely by the founder and current chairman of the Board (the Founder). Initially, the Company elected to be taxed as a subchapter S corporation and the Founder was responsible for federal and most state tax payments. On December 1, 2004, Restated Articles of Organization were adopted, and the Company authorized 8,000,000 shares of Series A Convertible Preferred Stock (the Redeemable Preferred Stock), par value $.01, increased the authorized number of shares of common stock, no par value, from 15,000 to 24,500,000, and changed to C corporation tax status. Effective October 18, 2006, the number of authorized shares of common stock was increased to 35,000,000.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers all highly liquid investments with a maturity date of three months or less when purchased to be cash equivalents. The Company accepts a range of debit and credit cards, and these transactions are transmitted to a bank for reimbursement within 24 hours, except for Friday and Saturday transactions, which are transmitted on Monday. The payments due from the banks for these debit and credit card transactions are generally received, or settle, within 24-48 hours of the transmission date. The Company considers all debit and credit card transactions that settle in less than seven days to be cash and cash equivalents. Amounts due from the banks for these transactions classified as cash and cash equivalents totaled $2,791 and $2,151 at December 31, 2006 and 2005, respectively.

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Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

Fair Value of Financial Instruments

The carrying amounts of financial instruments such as cash and cash equivalents, notes receivable, accounts payable, and other liabilities approximate fair value because of the short-term nature of these items. The carrying amounts of the equipment financing obligations and long-term debt approximate fair value because the interest rates on these instruments change with, or approximate, market interest rates.

Merchandise Inventories

The Company values merchandise inventories at the lower of cost or market. Merchandise cost is determined using the average cost method. All of the hardwood flooring purchased from vendors is either prefinished or unfinished, and in immediate saleable form. The Company adds the finish to, and boxes, various species of unfinished product, to produce certain proprietary products, primarily Bellawood, at its finishing facility. These finishing and boxing costs are included in the average unit cost of related merchandise inventory. The Company maintains an inventory reserve for loss or obsolescence, based on historical results and current sales trends. This reserve was $674 and $539 at December 31, 2006 and 2005, respectively.

Impairment of Long-Lived Assets

The Company evaluates potential impairment losses on long-lived assets used in operations when events and circumstances indicate that the assets may be impaired, and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amounts of those assets. If impairment exists and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amount of those assets, an impairment loss is recorded based on the difference between the carrying value and fair value of the assets. During 2004, the Company relocated its Corporate Headquarters and recorded an impairment charge of $293, primarily representing the remaining net asset value of the finishing equipment and leasehold improvements idled at the previous facility.

Goodwill

In 2004, the Company acquired the remaining 50% of the stock of its subsidiary, Hardwood Holdings LLC, for a cash payment of $1,050 and the forgiveness of amounts owed to the Company. The amount of the purchase price in excess of the carrying value of the minority interest liability of $1,050 was recorded as goodwill and is included within other assets. The Company evaluates goodwill for impairment on an annual basis, or whenever events or changes in circumstance indicate that the carrying value may be impaired. Based on the analysis performed, the Company has concluded that no impairment in the value of goodwill has occurred.

Recognition of Net Sales

The Company recognizes net sales for products purchased at the time the customer takes possession of the merchandise. Service revenue, primarily freight charges for in-home delivery, is recognized when the service has been rendered. Net sales are reduced by an allowance for anticipated sales returns based on historical and current sales trends and experience. The sales returns allowance and related changes were not significant for 2006, 2005 or 2004.

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

The Company generally requires customers to pay a deposit, equal to approximately 50% of the retail sales value, when purchasing merchandise inventories not regularly carried in a given store location, or not currently in stock. These deposits are included in Customer Deposits and Store Credits until the customer takes possession of the merchandise.

Cost of Sales

The cost of sales includes the actual cost of the merchandise sold, the transportation costs from vendor to the Company s distribution center or store location, any applicable finishing costs related to production of the Company s proprietary brand, the transportation costs from the distribution center to the store locations, and any inventory adjustments, including shrinkage.

The Company includes transportation costs for the delivery of products directly from stores to customers in cost of sales if delivered by third parties or in selling, general and administrative expenses (or SG&A) if delivered by the Company s delivery fleet. Costs related to the Company s delivery fleet, which include delivery salaries, maintenance and depreciation, totaled approximately $1,500 in 2006 and $2,400 for both 2005 and 2004.

The Company offers a range of prefinished products with warranties on the durability of the finish ranging from 10 to 50 years. Warranty reserves are based primarily on claims experience, sales history and other considerations, and warranty costs are recorded in the cost of sales. Warranty costs and changes to the warranty reserve were not significant for the years 2006, 2005 or 2004.

Advertising Costs

Advertising costs charged to SG&A were $36,288, $27,570 and $20,121 in 2006, 2005 and 2004, respectively. The Company uses various types of media to brand its name and advertise its products. Media production costs are generally expensed as incurred, except for direct mail, which is expensed when the finished piece enters the postal system. Media placement costs are generally expensed in the month the advertising occurs, except for contracted endorsements and sports agreements, which are generally expensed ratably over the contract period. Amounts paid in advance under endorsement contracts are included in prepaid expenses, and totaled $2,667 and $1,021 at December 31, 2006 and 2005, respectively.

Store Opening Costs

Costs to open new store locations are charged to SG&A as incurred.

Depreciation and Amortization

Property and equipment is carried at cost and depreciated on the straight-line method over the estimated useful lives of the related assets. Vehicles and office equipment are depreciated over useful lives which range from three to five years, and finishing equipment is depreciated over five years. The estimated useful lives for leasehold improvements are the shorter of the estimated useful lives or the remainder of the lease terms. For leases with optional renewal periods, the Company uses the original lease term, excluding optional renewal periods to determine the appropriate estimated useful lives. Leasehold improvements are currently being amortized over useful lives which range from two to fifteen years.

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Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

Some of the Company s vehicles and finishing equipment are leased under capital leases. These assets are recorded at the lower of fair value or the present value of net minimum lease payments and amortized over the shorter of their estimated useful life or the life of the lease. Amortization of capital leases is included within depreciation expense.

Operating Leases

The Company has operating leases for its stores, Corporate Headquarters and certain transportation equipment. The lease agreements for certain stores contain rent escalation clauses and rent holidays. For scheduled rent escalation clauses during the lease terms or for rental payments commencing at a date other than the date of initial occupancy, the Company records minimum rental expenses on a straight-line basis over the terms of the leases in SG&A.

Stock-Based Compensation

The Company adopted the provisions of Statement of Financial Accounting Standards (or SFAS) No. 123 (revised in 2004), Share-Based Payment (or SFAS 123 (R)), using the prospective-transition method effective January 1, 2006. Prior to the adoption of SFAS 123 (R), the Company used the intrinsic value method under the provisions of Accounting Principles Board Opinion No. 25 (or APB 25). There were no material differences in the calculations of the Company s stock-based compensation expense under APB 25 and SFAS 123, Accounting for Stock-Based Compensation in 2005 or 2004.

The Company maintains several equity incentive plans under which it may grant non-qualified stock options and incentive stock options to employees and non-employee directors. The Company recognizes expense for its stock-based compensation based on the fair value of the awards that are granted. Measured compensation cost is recognized ratably over the requisite service period of the related stock-based compensation award.

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

- Expected life of 7.5 years.
- Expected stock price volatility of 35%, based on the median volatility of companies in a peer group.
- Risk free interest rates from 4.6% to 5.2%.
- Dividends are not expected to be paid in any year.

Stock-based compensation awards that may be settled in cash are accounted for as liabilities and recorded at intrinsic value as prescribed in SFAS 123 (R).

Income Taxes

Income taxes are accounted for in accordance with SFAS No. 109, Accounting for Income Taxes (or SFAS 109). Income taxes are provided for under the asset and liability method and consider differences between the tax and financial accounting bases. The tax effects of these differences are

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

reflected on the balance sheet as deferred income taxes and valued using the effective tax rate expected to be in effect when the differences reverse. SFAS 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion of the deferred tax asset will not be realized. In evaluating the need for a valuation allowance, the Company took into account various factors, including the expected level of future taxable income. If actual results differ from the assumptions made in the evaluation of the valuation allowance, a change in the valuation allowance will be recorded through income tax expense in the period such determination is made.

In December 2004, the Company became a C corporation and income taxes have been provided since that date. The effect of initially recognizing deferred tax assets and liabilities related to this change in tax status was included in the provision for income taxes (benefit) for the year ended December 31, 2004.

Net Income per Common Share

Basic net income per common share is determined by dividing net income by the weighted average number of common shares outstanding during the year. Diluted net income per common share is determined by dividing net income by the weighted average number of common shares outstanding during the year, plus the dilutive effect of common share equivalents, such as stock options, warrants and preferred stock. Common shares and common share equivalents included in the computation represent shares issuable upon assumed exercise of outstanding stock options and warrants and the conversion of redeemable convertible preferred stock, except when the effect of their inclusion would be antidilutive.

Reclassifications

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

Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (or FASB) issued FASB Interpretation No. 48 (or FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS 109. FIN 48 describes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective as of January 1, 2007. The adoption of FIN 48 did not have a material effect on the Company s financial position or results of operations.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (or SFAS 157), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the impact of this pronouncement on its financial statements.

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (or SFAS 159). SFAS 159 permits entities to choose, at specified election dates, to measure eligible items at fair value (or fair value option) and to report in earnings unrealized gains and losses on those items for which the fair value option has been elected. SFAS 159 also requires entities to display the fair value of those assets and liabilities on the face of the balance sheet. SFAS 159 establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for the Company as of the first quarter of 2008. Early adoption is permitted. The Company is currently evaluating the impact of this pronouncement on its financial statements.

NOTE 2. NOTES RECEIVABLE

The Company has notes receivable from two key merchandise suppliers (together, the Vendor Notes) included in other assets on the balance sheets. One of the Vendor Notes, executed August 23, 2005 (the 2005 Note), consolidated several advances existing at that date, and matures in August 2009. The 2005 Note had an outstanding balance due to the Company of $701 and $880 at December 31, 2006 and 2005, respectively, of which $209 and $180, respectively, have been included in other current assets on the balance sheets. On August 15, 2006, the Company established two additional Vendor Notes with an original aggregate value of $1,265 (the 2006 Notes), maturing in February 2008. At December 31, 2006, the 2006 Notes had an outstanding balance due to the Company of $1,079, of which $800 has been included in other current assets.

NOTE 3. PROPERTY AND EQUIPMENT

Property and equipment consisted of:

	December 31, 2006	December 31, 2005
Vehicles	$ 7,633	$ 7,317
Finishing Equipment	3,151	3,097
Office Equipment	3,053	1,807
Store Fixtures	991	500
Leasehold Improvements	817	298
	15,645	13,019
Less: Accumulated Depreciation and Amortization	6,313	3,504
Property and Equipment, net	$ 9,332	$ 9,515

As of December 31, 2006 and 2005, property and equipment, net included assets under capital leases of $339 and $578, respectively, net of accumulated amortization of $1,410 and $1,171, respectively.

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

NOTE 4. LONG-TERM DEBT

Long-term debt consisted of the following:

	December 31, 2006	December 31, 2005
Consolidated Term Note	$ 8,398	$
Revolving Line of Credit	745	
Term Loan		4,000
Equipment Line of Credit		5,411
Other Notes Payable	140	233
	9,283	9,644
Less: Current Portions of Long-Term Debt	2,804	2,450
Total Long-Term Debt	$ 6,479	$ 7,194

On March 23, 2006, the Company entered into a loan agreement (the 2006 Loan Agreement) which consolidated the then existing term loan and equipment line of credit into one, $9,881 consolidated term note (the Consolidated Term Note) and provided a $5,000 revolving line of credit (the Revolver). Availability under the Revolver was increased to $10,000 on July 31, 2006. The 2006 Loan Agreement is secured by the Company s inventory and bears interest, payable monthly in arrears, at a variable rate, adjusted annually, based on the Company s performance under certain specified operating ratios. From inception to December 31, 2006, the 2006 Loan Agreement bore interest at the 30-Day London Interbank Offered Rate (LIBOR) + 0.90%. The 2006 Loan Agreement includes certain financial covenants that, among other things, require the Company to meet certain defined financial ratios, on a quarterly basis. The Company is in compliance with these financial covenants at December 31, 2006.

The Consolidated Term Note requires 60 equal, monthly principal payments, which began April 1, 2006 and conclude on March 1, 2011. The Revolver has no mandated payment provisions and expires on May 31, 2008. The Revolver has no restrictions on the mix of borrowings to letters of credit, other than the aggregate limit of $10,000. The Company primarily uses draws on the Revolver and letters of credit to fund international inventory purchases and has classified the entire balance as current at December 31, 2006. The Company had outstanding commitments under letters of credit of $2,018 at December 31, 2006. At December 31, 2006, $7,237 was available to borrow under the Revolver. The Company pays a fee of 0.25% per annum on any unused portion of the Revolver.

Prior to the 2006 Loan Agreement, the Company had a term loan, an equipment line of credit and a $5,000 revolving facility under an agreement executed in April 2004 (the 2004 Loan Agreement). The 2004 Loan Agreement also bore variable interest dependent on the Company s performance under certain defined financial ratios and at December 31, 2005, bore interest at LIBOR plus 1.25%. Interest rates under the 2004 Loan Agreement were generally higher in 2004 in comparison to 2005 and 2006, with the term loan and equipment line of credit bearing interest of LIBOR plus 1.50% at December 31, 2004.

Interest payments totaled $672, $574 and $417 in 2006, 2005 and 2004, respectively.

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

At December 31, 2006, scheduled maturities of long-term debt were: $2,804 in 2007; $2,033 in 2008; $1,976 in 2009; $1,976 in 2010; and $494 in 2011.

The Company believes the carrying amount of the long-term debt approximates fair value as the stated, variable interest rates approximate market rates.

NOTE 5. REDEEMABLE PREFERRED STOCK

In December 2004, a private investment group (the Investors) purchased 7,952,018 shares of Redeemable Preferred Stock for $35,000, or approximately $4.40 per share (the Preferred Sale). In conjunction with the sale of the Redeemable Preferred Stock, a 150,000 to 1 common stock dividend was declared and distributed to the Founder. Of the proceeds received from the sale of the Redeemable Preferred Stock, the Company retained $5,000 for general working capital purposes and $30,000 was paid to the Founder in the form of a cash distribution. To complete the Preferred Sale, the Company incurred and capitalized costs of $307, which are ratably accreted to interest through December 2010.

On or after December 6, 2010, any or all holders of the Redeemable Preferred Stock may elect to have the Company redeem the shares at $4.40 per share, plus any dividends declared but unpaid at the time of redemption. The Company cannot redeem shares of the Redeemable Preferred Stock at its discretion. At any time after December 6, 2004, either by election of an individual holder, or upon the holders of two-thirds of all the Redeemable Preferred Stock electing conversion, a share of Redeemable Preferred Stock is convertible, without additional consideration, into one share of common stock. Each share of Redeemable Preferred Stock has voting rights equivalent to a share of common stock, and any dividends declared must be distributed ratably among Common and Redeemable Preferred Stock, and the Investors are protected from dilution by certain defined provisions. Until redeemed or converted, the Redeemable Preferred Shares do not accrue any additional benefit.

NOTE 6. LEASES

The Company leases all store locations, the Corporate Headquarters and certain transportation equipment. The store location leases are operating leases and generally have five-year base periods with multiple five-year renewal periods.

The Founder is also the sole owner of ANO LLC, DORA Real Estate Company, LLC and Wood on Wood Road, Inc., and he has a 50% membership interest in BMT Holdings, LLC (collectively, ANO and Related Companies). The Company leased 26, 23 and 13 of its locations from ANO and Related Companies at December 31, 2006, 2005 and 2004 representing 28.6%, 30.3% and 22.8% of total store leases, respectively. The Company leases the Corporate Headquarters from ANO LLC under an operating lease with a base period through December 31, 2019.

Rental expense for 2006, 2005 and 2004 was $5,213, $4,425 and $2,347, respectively, with rental expense attributable to ANO and Related Companies of $2,261, $2,110 and $1,068, respectively.

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Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

The future minimum rental payments under capital leases and non-cancellable operating leases, segregating ANO and Related Companies leases from all other operating leases, were as follows at December 31, 2006:

		Operating Leases			
		ANO and Related Companies			Total
	Capital Leases	Store Leases	Headquarters Lease	Other Leases	Operating Leases
2007	$ 269	$ 1,189	$ 974	$ 3,385	$ 5,548
2008	60	1,094	1,003	3,139	5,236
2009	1	698	1,033	2,496	4,227
2010		474	1,064	1,819	3,357
2011		121	1,096	957	2,174
Thereafter			10,040	802	10,842
Total minimum lease payments	330	$ 3,576	$ 15,210	$ 12,598	$ 31,384
Less: amounts representing interest costs	(10)				
Present value of minimum lease payments	320				
Less: current maturities	(261)				
Long-term capital lease obligations	$ 59				

NOTE 7. STOCK BASED COMPENSATION

Total stock-based compensation expense was $1,449, $3,306 and $3,024 for 2006, 2005 and 2004, respectively. The Company maintains:

i) a stock option plan for executive management, the 2004 Stock Option and Grant Plan, as amended October 18, 2006 (the 2004 Option Plan),

ii) a stock option plan for non-employee members of the Board, the 2006 Equity Plan for Non-Employee Directors, as amended October 18, 2006 (the 2006 Director Plan), and

iii) a stock unit plan for regional store management, the 2006 Stock Unit Plan for Regional Managers (the 2006 Regional Plan).

The Company has reserved a total of 2.3 million shares of common stock to provide for the exercise of options under the 2004 Option Plan and the 2006 Director Plan. Under the 2006 Regional Plan, 85,000 stock units are outstanding and no additional grants are available.

The Company is also a party to a stock-based agreement between the Founder and his brother, Kevin Sullivan, a regional manager (or Kevin), accounted for as a variable performance plan (the Variable Plan). The Variable Plan was established in 1998, and modified in August 2005. In addition, the Company had a stock warrant plan (the Warrant Plan), established in 2004, with a senior executive who separated from the Company in May 2006 (the Former Executive).

In 2006, the Company granted the first stock options under the 2004 Option Plan. 952,691 stock options were granted in July (the July Grant) and 765,000 stock options were granted in October (the

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

October Grant). The stock options granted in July 2006 carry an exercise price of $7.58, the fair value of the Company on a fully diluted per share basis, and vest over a four year period, except in the event of the Company s initial public offering (the IPO), in which case the vesting is accelerated by one year. The stock options granted in October 2006 carry an exercise price of $7.83, the fair value of the Company on a fully diluted per share basis, vest over a four year period, but generally do not have vesting acceleration due to the IPO. The stock options under the 2004 Option Plan expire 10 years from the grant date. The fair value of the July Grant and October Grant were determined to be $3.74 and $3.75 per option, respectively, and stock-based compensation expense for these grants totaled $631 in 2006. As of December 31, 2006, the intrinsic value of these options totaled $3,303 and the weighted average remaining contractual term was 9.7 years.

In conjunction with the July Grant, the Company granted 79,156 stock options under the 2006 Director Plan. These stock options also carry an exercise price of $7.58, vest over a four year period, include a vesting acceleration for the IPO and expire 10 years from the grant date. Stock-based compensation expense for this grant totaled $37 in 2006. As of December 31, 2006, the intrinsic value of these options totaled $156 and the weighted average remaining contractual term was 9.5 years.

At December 31, 2006, no stock options were exercisable under either the 2004 Option Plan or the 2006 Director Plan.

The Founder will contribute the 85,000 shares of common stock necessary to provide for the exercise of the 85,000 stock units granted under the 2006 Regional Plan in July and outstanding at December 31, 2006. The stock units vest over a five year period, but expire without value unless the IPO or a sale event, as defined, occur prior to the mandatory redemption of the Redeemable Preferred Stock for cash at the Conversion Price. As such, the Company has not recorded compensation expense related to the 2006 Regional Plan as of December 31, 2006.

The Variable Plan, as modified in August 2005, awarded Kevin the right (the Variable Right) to a fixed ownership percentage of 2.5% on a fully diluted basis, plus an additional ownership percentage based on certain performance criteria, primarily a comparison of the net income of the region under Kevin s management to total Company net income on a trailing twelve-month basis. The Variable Right is exercisable for shares of common stock, contributed by the Founder, in conjunction with the IPO or a sale event, as defined. On February 1, 2008, the Variable Plan allows for a cash settlement of the Variable Right at a defined, performance based, value through put-call provisions, which may be executed by either the Founder or Kevin. The Founder is liable for the cash payment, and the Company guarantees the performance. Immediately prior to the completion of the IPO or sale event, however, the Variable Right is considered exercised in full, and any cash settlement provisions via put-call rights terminate.

Prior to the August 2005 modification of the Variable Plan, share based compensation expense was recorded based on Kevin having earned a 5% ownership interest on a fully diluted basis, again based primarily on the performance of the region under his management.

The Company recorded stock-based compensation expense under the Variable Plan of $1,040, $3,133 and $2,938 in 2006, 2005 and 2004, respectively, and carried a long-term liability of $9,132 and $8,092 at December 31, 2006 and 2005, respectively.

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Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

Under the Warrant Plan, the stock-based compensation expense of $173 and $86 in 2005 and 2004, respectively, was reversed in 2006 upon the Former Executive separating from the Company.

As of December 31, 2006 total unrecognized stock-based compensation expense related to nonvested stock options was approximately $6,060 and is expected to be recognized over a weighted average period of approximately 3.7 years.

NOTE 8. INCOME TAXES

The provision for income taxes consists of the following:

	Year Ended December 31,		
	2006	**2005**	**2004**
Current			
Federal	$ 7,433	$ 7,242	$
State	1,425	1,438	245
Total Current	8,858	8,680	245
Deferred			
Federal	(627)	(1,444)	(1,415)
State	(70)	(288)	(280)
Total Deferred	(697)	(1,732)	(1,695)
Total Provision for Income Taxes	$ 8,161	$ 6,948	$ (1,450)

The reconciliation of significant differences between income tax expense (benefit) applying the federal statutory rate of 35% and the actual income tax expense (benefit) at the effective rate are as follows:

	Year Ended December 31,		
	2006	**2005**	**2004**
Income tax expense at federal statutory rate	$ 7,299	$ 6,203	$ 2,291
Increases (decreases):			
State income taxes, net of federal income tax benefit	855	745	264
Effect of change in tax status			(3,994)
Other	7		(11)
Total	$ 8,161	$ 6,948	$ (1,450)

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Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

The tax effects of temporary differences that result in significant portions of the deferred tax accounts are as follows:

	December 31, 2006	December 31, 2005
Deferred Tax Liabilities:		
Prepaid Expenses	$ (290)	$
Depreciation and Amortization	(241)	(578)
Total Deferred Tax Liabilities	(531)	(578)
Deferred Tax Assets:		
Stock Compensation Expense	3,797	3,279
Reserves	677	608
Other	181	118
Total Deferred Tax Assets	4,655	4,005
Net Deferred Tax Asset	$ 4,124	$ 3,427

The Company made income tax payments of $6,989, $10,381 and $109 in 2006, 2005 and 2004, respectively.

NOTE 9. PROFIT SHARING PLAN

The Company maintains a profit-sharing plan, qualified under Section 401(k) of the Internal Revenue Code, for all eligible employees. Employees are eligible to participate following the completion of one year of service and attainment of age 21. The Company matches 50% of employee contributions up to 6% of eligible compensation. The Company s matching contributions, included in SG&A, totaled $160, $124 and $68 in 2006, 2005 and 2004, respectively.

NOTE 10. NET INCOME PER COMMON SHARE

The following table sets forth the computation of basic and diluted net income per common share:

	Year Ended December 31, 2006	2005	2004
Net Income	$ 12,898	$ 10,713	$ 7,986
Weighted Average Common Shares Outstanding Basic	15,000,100	15,000,100	15,000,100
Effect of Dilutive Securities:			
Redeemable Preferred Stock	7,952,018	7,952,018	675,377
Warrants	37,285	111,056	

Weighted Average Common Shares Outstanding Diluted	22,989,403	23,063,174	15,675,477
Net Income per Common Share Basic	$ 0.86	$ 0.71	$ 0.53
Net Income per Common Share Diluted	$ 0.56	$ 0.46	$ 0.51

The Company s calculation of diluted net income per common share in 2006 and 2005 included the dilutive impact of common stock warrants under the Warrant Plan. For 2006, options to purchase 1,796,847 shares of common stock were not included in the computation of Weighted Average Common Shares Outstanding Diluted because the effect would be antidilutive. There were no options outstanding prior to July 2006.

Lumber Liquidators, Inc.

Notes to Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

NOTE 11. RELATED PARTY TRANSACTIONS

As described in Note 6, the Company leases a number of its store locations and Corporate Headquarters from ANO and Related Companies.

As of December 31, 2006, other assets included $35 that the Founder owed the Company in the normal course of business. The amount was paid in the first quarter of 2007.

In 2005 and pursuant to the terms of the Preferred Sale, the Founder assumed a net liability related to a capitalized lease, and the Company recorded a $581 contribution from the Founder.

In 2004, the Company distributed a net $41,934 to the Founder, including $11,934 of distributions primarily related to the Company s status as an S corporation and a $30,000 distribution related to the Preferred Sale.

NOTE 12. COMMITMENTS AND CONTINGENCIES

In July 2006, the Company entered into a purchase agreement with a vendor where the Company would purchase a total of approximately 27 million square feet of the vendor s assorted products over a four-year period, with the unit prices set at the time a purchase order is created/accepted.

Legal Proceedings

On January 4, 2007, Clifford Wayne Bassett and Clifford Wayne Bassett, MD, PC (together Dr. Bassett) filed a lawsuit entitled *Clifford Wayne Bassett et al. v. Lumber Liquidators, Inc. et al.*, in the U.S. District Court for the Southern District of New York, against the Company, E.W. Scripps Company (Scripps) and others. The Company purchased an article from Scripps describing the benefits of hardwood flooring in relation to other types of flooring. The article contained a quote by Dr. Basset, an allergist, who claims that the use of the quote was unauthorized. Dr. Basset has asserted damages in excess of $10 million. The matter is in the early stages of litigation and, while there is a reasonable possibility that a material loss may be incurred, the Company cannot estimate the loss, if any, at this time. In connection with SFAS No. 5, Accounting for Contingencies (or SFAS 5) paragraph 8, we have not made any provision in connection with this matter. The Company intends to defend vigorously against this claim and, to the extent warranted, to seek contribution or indemnification from other parties.

The Company received a demand letter dated December 22, 2006, from counsel representing the Former Executive in connection with his resignation of employment on May 31, 2006. In the letter, counsel for the Former Executive requested that documents related to the executive be preserved. When he terminated his employment, the Former Executive asserted that he did so for good reason , as defined within his employment agreement and the Warrant Plan. Under the provisions of his employment agreement, his termination for good reason would entitle him to 2 years of wages and benefits, and under the provisions of the Warrant Plan, he would be entitled to 1% of the outstanding common stock. In June 2006, the Company responded to the Former Executive that his contention regarding his termination for good reason was erroneous. The Former Executive has not filed a lawsuit or a demand for arbitration. While there is a reasonable possibility that a material loss may be incurred, the Company cannot estimate the loss, if any, at this time. In connection with SFAS 5 paragraph 8, we have not made any provision in connection with this matter. The Company intends to defend vigorously against any claim brought in connection with this matter.

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Lumber Liquidators, Inc.

Notes to the Financial Statements (Continued)

(amounts in thousands, except share data and per share amounts)

The Company is from time to time subject to claims and disputes arising in the normal course of business. In the opinion of management, while the outcome of any such claims and disputes cannot be predicted with certainty, the ultimate liability of the Company in connection with these matters is not expected to have a material adverse effect on the Company s results of operations, financial position or cash flows.

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Lumber Liquidators, Inc.

Condensed Balance Sheets

(in thousands, except share data)

	September 30, 2007 (unaudited)	December 31, 2006
Assets		
Current Assets:		
Cash and Cash Equivalents	$ 5,666	$ 3,965
Merchandise Inventories	74,944	51,758
Prepaid Expenses	3,172	3,638
Other Current Assets	3,410	3,359
Total Current Assets	**87,192**	**62,720**
Property and Equipment, net	11,381	9,332
Deferred Income Taxes	5,337	3,737
Other Assets	2,485	2,231
Total Assets	**$ 106,395**	**$ 78,020**
Liabilities and Shareholder s Equity (Deficit)		
Current Liabilities:		
Accounts Payable	$ 20,740	$ 16,296
Customer Deposits and Store Credits	10,184	6,804
Stock Compensation Liability	12,034	
Accrued Compensation	2,580	1,566
Other Current Liabilities	7,640	5,292
Current Portion of Long-Term Debt and Capital Lease Obligations	9,328	3,065
Total Current Liabilities	**62,506**	**33,023**
Long-Term Debt and Capital Lease Obligations	4,947	6,538
Stock Compensation Liability		9,132
Redeemable Preferred Stock	34,834	34,795
Stockholder s Equity (Deficit):		
Common stock ($0.001 and no par value, respectively; 35,000,000 authorized; 15,000,100 issued and outstanding)	15	
Additional Capital	2,533	1,250
Retained Earnings (Deficit)	1,560	(6,718)
Total Stockholder s Equity (Deficit)	**4,108**	**(5,468)**
Total Liabilities and Stockholder s Equity (Deficit)	**$ 106,395**	**$ 78,020**

See accompanying notes to condensed financial statements

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Lumber Liquidators, Inc.

Condensed Statements of Income

(in thousands, except share data and per share amounts)

(unaudited)

	Three months ended September 30, 2007	Three months ended September 30, 2006	Nine months ended September 30, 2007	Nine months ended September 30, 2006
Net Sales	**$ 102,050**	**$ 83,090**	**$ 299,797**	**$ 247,219**
Cost of Sales	67,603	55,688	200,404	163,955
Gross Profit	**34,447**	**27,402**	**99,393**	**83,264**
Selling, General and Administrative Expenses	28,260	22,587	85,491	64,611
Operating Income	**6,187**	**4,815**	**13,902**	**18,653**
Interest Expense	252	210	607	548
Other (Income) Expense	(68)	(123)	(168)	(303)
Income Before Income Taxes	**6,003**	**4,728**	**13,463**	**18,408**
Provision for Income Taxes	2,302	1,832	5,185	7,133
Net Income	**$ 3,701**	**$ 2,896**	**$ 8,278**	**$ 11,275**
Net Income per Common Share Basic	**$ 0.25**	**$ 0.19**	**$ 0.55**	**$ 0.75**
Net Income per Common Share Diluted	**$ 0.16**	**$ 0.13**	**$ 0.36**	**$ 0.49**
Weighted Average Common Shares Outstanding:				
Basic	15,000,100	15,000,100	15,000,100	15,000,100
Diluted	23,233,770	22,952,118	23,096,460	23,001,681

See accompanying notes to condensed financial statements

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Lumber Liquidators, Inc.

Condensed Statements of Cash Flows

(in thousands)

(unaudited)

	Nine months ended September 30, 2007	Nine months ended September 30, 2006
Cash Flows from Operating Activities:		
Net Income	$ 8,278	$ 11,275
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	2,605	2,118
Deferred Income Taxes	(1,600)	(1,022)
Stock-Based Compensation Expense	4,200	764
Accretion of Redeemable Preferred Stock	39	39
Changes in Operating Assets and Liabilities:		
Merchandise Inventories	(23,186)	(22,312)
Accounts Payable	4,444	5,808
Customer Deposits and Store Credits	3,380	(18)
Prepaid Expenses and Other Current Assets	2,053	771
Other Assets and Liabilities	3,210	3,461
Net Cash Provided by Operating Activities	**3,423**	**884**
Cash Flows from Investing Activities:		
Purchases of Property and Equipment	(4,756)	(2,074)
Net Cash Used in Investing Activities	**(4,756)**	**(2,074)**
Cash Flows from Financing Activities:		
Proceeds from Long-Term Borrowings and Revolving Line	6,425	1,079
Repayments of Long-Term Borrowings and Revolving Line	(1,543)	(1,258)
Payments of IPO Costs	(1,638)	
Principal Payments on Capital Lease Obligations	(210)	(306)
Net Cash Provided by (Used in) Financing Activities	**3,034**	**(485)**
Net Increase (Decrease) in Cash and Cash Equivalents	1,701	(1,675)
Cash and Cash Equivalents, Beginning of Period	3,965	6,031
Cash and Cash Equivalents, End of Period	**$ 5,666**	**$ 4,356**

See accompanying notes to condensed financial statements

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Lumber Liquidators, Inc.

Notes to Condensed Financial Statements

(amounts in thousands, except share data and per share amounts)

(unaudited)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

Lumber Liquidators, Inc. (or the Company) is a multi-channel specialty retailer of hardwood flooring, and hardwood flooring enhancements and accessories, operating as a single business segment. The Company offers an extensive assortment of exotic and domestic hardwood species, engineered hardwoods, and laminates direct to the consumer. The Company also features the renewable flooring products bamboo and cork, and provides a wide selection of flooring enhancements and accessories, including moldings, noise-reducing underlay and adhesives. These products are primarily sold under the Company s private label brands, including the premium Bellawood floors. The Company sells primarily to homeowners or to contractors on behalf of homeowners through a network of stores located in primary or secondary metropolitan areas throughout the United States. In addition to the store locations, the Company s products may be ordered, and customer questions/concerns addressed, through both our call center in Toano, Virginia, and our website, LumberLiquidators.com. The Company finished the majority of the Bellawood products in Toano, Virginia, which along with the call center, corporate offices and distribution facility represent the Corporate Headquarters.

Organization and Basis of Financial Statement Presentation

The Company was organized in 1994 as a Massachusetts corporation. On August 28, 2007, the Company was reincorporated in Delaware. As a Massachusetts corporation the Company s stock maintained no par value. As a result of the reincorporation in Delaware, the par value was increased to $0.001 per share.

The unaudited condensed financial statements included in this quarterly report have been prepared by the Company according to the rules and regulations of the Securities and Exchange Commission (or SEC) and according to accounting principles generally accepted in the United States of America (or GAAP) for interim financial statements. The accompanying balance sheet information as of December 31, 2006 is derived from our audited financial statements. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been omitted in accordance with the SEC s rules and regulations for interim financial statements. The financial statements reflect, in the opinion of management, all adjustments which consist solely of normal recurring adjustments necessary to present fairly the Company s financial position and results of operations as of and for the periods indicated. Certain reclassifications have been made to conform prior year classifications to the current year presentation.

The results of operations for the three and nine months ended September 30, 2007 are not necessarily indicative of the results of operations that may be achieved for the full year.

The unaudited condensed financial statements included in this quarterly report should be read in conjunction with the audited financial statements and related footnotes included in the Form S-1 filed with the SEC.

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Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (or FASB) issued FASB Interpretation No. 48 (or FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS 109. FIN 48 describes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 was effective as of January 1, 2007. The adoption of FIN 48 did not have a material effect on the Company s financial position or results of operations.

In September 2006, the FASB issued Statement of Financial Accounting Standards (or SFAS) No. 157, Fair Value Measurements (or SFAS 157), which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the impact of this pronouncement on its financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (or SFAS 159). SFAS 159 permits entities to choose, at specified election dates, to measure eligible items at fair value (or fair value option) and to report in earnings unrealized gains and losses on those items for which the fair value option has been elected. SFAS 159 also requires entities to display the fair value of those assets and liabilities on the face of the balance sheet. SFAS 159 establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for the Company as of the first quarter of 2008. Early adoption is permitted. The Company is currently evaluating the impact of this pronouncement on its financial statements.

NOTE 2. NOTES RECEIVABLE

In June 2007, the Company consolidated two outstanding notes receivable from merchandise suppliers (the 2006 Notes) into one note with an aggregate value of $912 (the 2007 Note), maturing in June 2010. A separate note (the 2005 Note), which matures in August 2009, was not modified. As of December 31, 2006, the 2007 Note and the 2005 Note (together, the Vendor Notes) had an outstanding balance due to the Company of $1,780, of which $1,009 had been included in other current assets. As of September 30, 2007, the Vendor Notes had an outstanding balance of $1,415 due to the Company of which $546 has been included in other current assets.

NOTE 3. LONG-TERM DEBT

Long-term debt consisted of the following:

	September 30, 2007	December 31, 2006
Consolidated Term Note	$ 6,917	$ 8,398
Revolving Line of Credit	7,170	745
Other Notes Payable	78	140
	14,165	9,283
Less: Current Portions of Long-Term Debt	9,225	2,804
Total Long-Term Debt	$ 4,940	$ 6,479

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The Consolidated Term Note requires 60 equal, monthly principal payments, which began April 1, 2006 and conclude on March 1, 2011. The Consolidated Term Note is secured by the Company s inventory and bears interest, payable monthly in arrears, at a variable rate, adjusted annually, based on the Company s performance under certain specified operating ratios. The Consolidated Term Note bears interest at the 30-Day London Interbank Offered Rate (LIBOR) (floating daily) + 0.90%. The Loan Agreement includes certain financial covenants that, among other things, require the Company to meet certain defined financial ratios on a quarterly basis. The Company is in compliance with these financial covenants at September 30, 2007.

The Company primarily uses draws on the revolving line of credit to fund inventory purchases and general operations. On August 10, 2007, the Company entered into a new revolving credit agreement (or 2007 Revolver) to replace the existing revolving line of credit (the 2006 Revolver), which provided for borrowings up to up to $10,000 and was set to expire on May 31, 2008. The 2007 Revolver provides for borrowings up to $25,000 and expires on August 10, 2012. The 2007 Revolver allows for letters of credit up to $5,000, has no mandated payment provisions and the Company pays a fee of 0.125% per annum, which may be increased in the future based on financial performance criteria, on any unused portion of the Revolver. Amounts outstanding under the 2007 Revolver are subject to an interest rate of LIBOR (reset on the 10th of the month) + 0.50%, which may increase based on financial performance criteria. The 2006 Revolver bore interest at the 30-Day LIBOR + 0.90%, and the Company paid a fee of 0.25% per annum on any unused portion of the Revolver. The 2007 Revolver has certain defined covenants and restrictions, including the maintenance of certain defined financial ratios. The Company is in compliance with these financial covenants at September 30, 2007. As of September 30, 2007 the Company had $7,170 outstanding on the 2007 Revolver which was classified as current and $17,830 was available to borrow.

NOTE 4. STOCK-BASED COMPENSATION

Total stock-based compensation expense was $290 and $4,200 for the three and nine months ended September 30, 2007, respectively. Total stock-based compensation expense was $504 and $765 for the three and nine months ended September 30, 2006, respectively. The Company:

i) maintains a stock option plan for employees, non-employee directors and other service providers, the Lumber Liquidators, Inc. 2007 Equity Compensation Plan (the 2007 Plan),

ii) is a party to a stock-based agreement between the Founder and his brother, Kevin Sullivan, a regional manager (or Kevin), accounted for as a variable performance plan (the Variable Plan), and

iii) maintains a stock unit plan for regional store management, the 2006 Stock Unit Plan for Regional Managers (the 2006 Regional Plan).

In August 2007, the Company adopted and the shareholders approved the 2007 Plan. The number of shares of common stock authorized for issuance with respect to awards granted under the 2007 Plan is 4.3 million, reduced by (i) any shares that have been issued under either the 2004 Stock Option and Grant Plan and the 2006 Equity Plan for Non-Employee Directors (collectively, the Prior Plans), and (ii) any shares that are subject to outstanding awards under the Prior Plans that have not been forfeited or canceled. No additional options will be issued under the Prior Plans. Stock options granted under the 2007 Plan expire no later than ten years from the date of grant and the exercise price shall not be less than the fair market value of the shares on the date of grant. Vesting periods are assigned to stock options on a grant by grant basis at the discretion of the Board of Directors.

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Stock Options

The following is a summary of our stock option activity and related prices for the first nine months of 2007:

	Shares	Weighted Average Exercise Price	Remaining Average Contractual Term (Years)	Intrinsic Value
Balance, December 31, 2006	1,796,847	$ 7.69	8.9	$ 3,492
Granted	50,000	10.26	9.6	
Exercised				
Forfeited				
Balance, September 30, 2007	1,846,847	$ 7.76	8.9	$ 9,685
Exercisable at September 30, 2007	261,260	$ 7.58	8.9	$ 1,416

The aggregate intrinsic value is determined using a $13.00 per share estimated fair value of our common stock on September 30, 2007, as determined by management. Management s estimate was based on the Company s estimated fair value as a public entity. During the nine months ended September 30, 2007, no stock options were exercised.

As of September 30, 2007, total unrecognized compensation cost related to unvested options was approximately $5,024, net of estimated forfeitures, which we expect to recognize over a weighted average period of approximately 2.9 years.

The fair value of each stock option award is estimated by management on the date of the grant using the Black-Scholes-Merton option pricing model. The weighted average fair value of options granted during the nine months ended September 30, 2007 and 2006 were $10.26 and $7.58,respectively.

The following are the weighted average assumptions for the periods noted:

	Nine Months ended September 30, 2007	Nine Months ended September 30, 2006
Expected dividend rate	Nil	Nil
Expected stock price volatility range	39%	35%
Risk-free interest rate range	4.60%	5.23%
Expected life of options	7.5 years	7.5 years

The expected stock price volatility range is based on the historical volatilities of companies included in a peer group that was selected by management whose shares or options are publicly available. The volatilities are estimated for a period of time equal to the expected life of the related option. The risk-free interest rate is based on the implied yield currently available on U.S. Treasury zero-coupon issues with an equivalent remaining term. The expected life of the options was determined using a lattice model to estimate the expected term as an input into the Black-Scholes-Merton closed-form model.

The Company recorded stock-based compensation expense related to stock options of $440 and $1,298 for the three and nine months ended September 30, 2007, respectively. The Company recorded stock-based compensation expense related to stock options of $244 for the three and nine months ended September 30, 2006.

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Stock options outstanding and exercisable as of September 30, 2007 are summarized below:

	Outstanding			Exercisable	
Range of Exercise Prices	Number of Option Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Number of Option Shares	Weighted Average Exercise Price
$ 7.58 $7.83	1,796,847	$ 7.69	8.9	261,260	$ 7.58
$10.26	50,000	10.26	9.6		
Balance, September 30, 2007	1,846,847	$ 7.76	8.9	261,260	$ 7.58

Variable Performance Plan

The Company is also a party to a stock-based agreement between the Founder and his brother, Kevin Sullivan, a regional manager (or Kevin), accounted for as a variable performance plan (the Variable Plan). The Variable Plan was established in 1998 and modified in August 2005. The Variable Plan awarded Kevin the right (the Variable Right) to a fixed ownership percentage of 2.5% on a fully diluted basis, plus an additional ownership percentage based on certain performance criteria, primarily a comparison of the net income of the region under Kevin s management to total Company net income on a trailing twelve-month basis. The Variable Right is exercisable for shares of common stock, contributed by the Founder, in conjunction with the IPO or a sale event, as defined, and immediately prior to the completion of the IPO or sale event, the Variable Right is considered exercised in full, and any cash settlement provisions via put-call rights terminate.

If an IPO or sale event, as defined, has not occurred prior to February 1, 2008, the Variable Plan allows for a cash settlement of the Variable Right at a defined, performance based, value through put-call provisions, which may be executed by either the Founder or Kevin. The Founder is liable for the cash payment, and the Company guarantees the performance.

The Company recorded stock-based compensation expense under the Variable Plan of $(150) and $2,902 for the three and nine months ended September 30, 2007, respectively and, due to the put-call provisions, carried a short-term liability of $12,034 as of September 30, 2007. The Company recorded stock-based compensation expense under the Variable Plan of $260 and $780 for the three and nine months ended September 30, 2006.

Stock Units

The Company has a stock unit plan for regional store management, the 2006 Stock Unit Plan for Regional Managers (the 2006 Regional Plan). The 2006 Regional Plan has 85,000 stock units outstanding and the Founder will contribute the 85,000 shares of common stock necessary to provide for the exercise of the stock units. No additional grants of stock units are available under the 2006 Regional Plan. The stock units vest over approximately a five year period, but expire without value unless the IPO or a sale event, as defined, occur, and as such, the Company has not recorded compensation expense related to the 2006 Regional Plan as of September 30, 2007.

Stock Warrants

The Company had a stock warrant plan (the Warrant Plan), established in 2004, with a senior executive who separated from the Company in May 2006. As a result of the separation during the second quarter of 2006, the Company reversed the $259 of compensation expense that had been previously recognized.

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NOTE 5. NET INCOME PER COMMON SHARE

The following table sets forth the computation of basic and diluted net income per common share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Net Income	$ 3,701	$ 2,896	$ 8,278	$ 11,275
Weighted Average Common Shares Outstanding Basic	15,000,100	15,000,100	15,000,100	15,000,100
Effect of Dilutive Securities				
Redeemable Preferred Stock	7,952,018	7,952,018	7,952,018	7,952,018
Stock Options	281,652		144,342	
Warrants				49,563
Weighted Average Common Shares Outstanding Diluted	23,233,770	22,952,118	23,096,460	23,001,681
Net Income Per Common Share Basic	$ 0.25	$ 0.19	$ 0.55	$ 0.75
Net Income Per Common Share Diluted	$ 0.16	$ 0.13	$ 0.36	$ 0.49

For the three and nine months ended September 30, 2007, options to purchase 50,000 shares of common stock that were granted in April 2007 were not included in the computation of Weighted Average Common Shares Outstanding Diluted because the effect would be antidilutive. For the three and nine months ended September 30, 2006, options to purchase 1,031,847 shares of common stock were not included in the computation of Weighted Average Common Shares Outstanding Diluted because the effect would be antidilutive. There were no warrants outstanding after the Former Executive separated from the Company in May 2006.

NOTE 6. RELATED PARTY TRANSACTIONS

As of September 30, 2007, the Company leases the Corporate Headquarters and 23 of its 111 other store locations from ANO LLC, a company that is wholly owned by the Founder. The Company leases one store location each from DORA Real Estate Company, LLC, Wood on Wood Road, Inc. and BMT Holdings, LLC. DORA Real Estate Company, LLC and Wood on Wood Road, Inc. are wholly owned by the Founder, and he has a 50% membership interest in BMT Holdings, LLC. Rental expense related to these companies for the three and nine months ended September 30, 2007 was $636 and $1,841, respectively. Rental expense related to these companies for the three and nine months ended September 30, 2006 was $560 and $1,673, respectively.

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NOTE 7. COMMITMENTS AND CONTINGENCIES

In July 2006, the Company entered into a purchase agreement with a vendor where the Company would purchase a total of approximately 27 million square feet of the vendor s assorted products over a four-year period, with the unit prices set at the time a purchase order is created/accepted. Certain disputes have arisen between the parties primarily with regard to product quality, unit price changes and delivery and payment obligations. The Company is not currently receiving product under the agreement and intends to seek payment for the Company s cover costs relating to purchase orders that were not delivered. The products ordered from the vendor that are not being delivered are available from other suppliers and the cover costs are expected to be immaterial.

Legal Proceedings

On January 4, 2007, Clifford Wayne Bassett and Clifford Wayne Bassett, MD, PC (together Dr. Bassett) filed a lawsuit entitled Clifford Wayne Bassett et al. v. Lumber Liquidators, Inc. et al., in the U.S. District Court for the Southern District of New York, against the Company, E.W. Scripps Company (Scripps) and others. The Company purchased an article from Scripps describing the benefits of hardwood flooring in relation to other types of flooring. The article contained a quote by Dr. Bassett, an allergist, who claims that the use of the quote was unauthorized. Dr. Bassett has asserted damages in excess of $10 million. The matter is in the early stages of litigation and, while there is reasonable possibility that a material loss may be incurred, the Company cannot estimate the loss, if any, at this time. In connection with SFAS No. 5, Accounting for Contingencies (or SFAS 5) paragraph 8, we have not made any provision in connection with this matter. The Company intends to defend vigorously against this claim and, to the extent warranted, seek contribution or indemnification from other parties.

On July 12, 2007, the Company received a copy of a Demand for Arbitration, dated July 11, 2007, in which a senior executive who separated from the Company in May 2006 (the Former Executive) contends that the Company breached its obligations to him upon his resignation of employment. The Former Executive alleges that he terminated his employment for good reason, as defined in his employment agreement and the Warrant Plan, based on an allegedly substantial reduction in his responsibilities. In his demand for arbitration, the Former Executive contends that the Company breached its obligations to him upon his resignation of employment. He is seeking damages of approximately $0.7 million (plus the value of certain other specified benefits), as well as a declaration that he has owned 1% of the Company since he terminated his employment. An arbitration hearing was held on October 1-2, 2007. The parties will be afforded the opportunity to submit post-arbitration briefs and additional testimony and evidence may be presented. While there is reasonable possibility that a material loss may be incurred, the Company cannot estimate the loss, if any, at this time. In connection with SFAS 5 paragraph 8, we have not made any provision in connection with this matter. The Company intends to defend itself vigorously against the Former Executive s claim.

The Company is from time to time subject to claims and disputes arising in the normal course of business. In the opinion of management, while the outcome of any such claims and disputes cannot be predicted with certainty, the ultimate liability of the Company in connection with these matters is not expected to have a material adverse effect on the Company s results of operations, financial position or cash flows.

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11,500,000 Shares

Lumber Liquidators, Inc.

Common Stock

PROSPECTUS

Goldman, Sachs & Co.

Merrill Lynch & Co.

Lehman Brothers

Banc of America Securities LLC

Piper Jaffray

No dealer, salesperson or other person is authorized to give any information or to represent anything not contained in this prospectus or any free writing prospectus prepared by us or on our behalf. You must not rely on any unauthorized information or representations. This prospectus is an offer to sell only the shares offered hereby, but only under circumstances and in jurisdictions where it is lawful to do so. The information contained in this prospectus is current only as of its date.

Through and including , 2007 (the 25th day after the date of this prospectus), all dealers effecting transactions in these securities, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to a dealer s obligation to deliver a prospectus when acting as an underwriter and with respect to an unsold allotment or subscription.

, 2007

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PART II

Information Not Required in Prospectus

Item 13. Other Expenses of Issuance and Distribution

The following table shows the costs and expenses, other than underwriting discounts and commissions, payable in connection with the issuance and distribution of the securities being registered. Except as otherwise noted, we will pay all of these amounts. All amounts except the SEC registration fee and the NASD filing fee are estimated.

SEC Registration Fee	5,685
NASD Filing Fee	24,015
NYSE Listing Fees	160,000
Accounting Fees and Expenses	850,000
Legal Fees and Expenses	1,200,000
Printing Fees and Expenses	200,000
Transfer Agent and Registrar Fees and Expenses	15,000
Blue Sky Fees and Expenses	15,000
Miscellaneous	30,300
Total	2,500,000

Item 14. Indemnification of Directors and Officers

Section 145 of the Delaware General Corporation Law authorizes a corporation to indemnify its directors, officers, employee and agents against expenses (including attorney s fees), judgments, fines and amounts paid in settlement reasonably incurred, provided they act in good faith and in a manner reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal proceeding, had no reasonable cause to believe their conduct was unlawful, although in the case of proceedings brought by or on behalf of the corporation, such indemnification is limited to expenses and is not permitted if the individual is adjudged liable to the corporation (unless the Delaware Court of Chancery or the court in which such proceeding was brought determines otherwise in accordance with the Delaware General Corporation Law). Section 102 of the Delaware General Corporation Law authorizes a corporation to limit or eliminate its directors liability to the corporation or its stockholders for monetary damages for breaches of fiduciary duties, other than for (i) breaches of the duty of loyalty; (ii) acts or omissions not in good faith or that involve international misconduct or knowing violations of law; (iii) unlawful payments of dividends, stock purchases or redemptions; or (iv) transactions from which a director derives an improper personal benefit. Our certificate of incorporation contains such a provision.

Our bylaws incorporate Section 145 of the Delaware General Corporation Law, which provides that we will indemnify each director and officer against all claims and expenses resulting from the fact that such person was an director, officer, agent or employee of the registrant. A claimant is eligible for indemnification if the claimant (i) acted in good faith and in a manner that, in the claimant s reasonable belief, was in or not opposed to the best interest of the registrant; or (ii) in the case of a criminal proceeding, had no reasonable cause to believe the claimant s conduct was unlawful. This determination will be made by our disinterested directors, our shareholders or independent counsel in accordance with Section 145 of the Delaware General Corporation Law.

Section 145 of the Delaware General Corporation Law authorizes a corporation to purchase and maintain insurance on behalf of any person who is or was a director, officer, employee or agent of the corporation against any liability asserted against and incurred by such person in any such capacity, or arising out of such person s status as such. We have obtained liability insurance covering our directors and officers for claims asserted against them or incurred by them in such capacity.

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The underwriting agreement between Lumber Liquidators and the underwriters (filed as exhibit 1.01 hereto) will provide that the underwriters are obligated, under certain circumstances, to indemnify our directors, officers and controlling persons against certain liabilities, including liabilities under the Securities Act. The registration rights agreement among Lumber Liquidators, TA Associates and the TA Associates Funds (filed as exhibit 10.13 hereto) provides that the TA Associates Funds are obligated, under certain circumstances, to indemnify our directors and officers against certain liabilities, including liabilities under the Securities Act. Pursuant to that agreement and other arrangements we expect to enter into, we may be obligated, under certain circumstances, to indemnify various parties including certain of our directors against certain liabilities, including liabilities under the Securities Act.

Reference is made to Item 17 for our undertakings with respect to indemnification for liabilities arising under the Securities Act.

Item 15. Recent Sales of Unregistered Securities

In the three years preceding the filing of this registration statement, we have sold and issued the following unregistered securities:

(1) On December 6, 2004, we issued an aggregate of 7,952,018 million shares of series A convertible preferred stock, par value $0.01, for an aggregate offering price of $35.0 million to TA IX L.P., TA/Atlantic and Pacific IV L.P., TA Strategic Partners Fund A L.P., TA Strategic Partners Fund B L.P. and TA Investors II L.P. The ultimate general partner or manager of each of such entity is TA Associates, Inc.

(2) On July 13, 2006, we granted 952,691 stock options relating to our common stock with an exercise price of $7.58 per share to certain members of our executive management under our 2004 Option Plan.

(3) On July 13, 2006, we granted 79,156 stock options relating to our common stock with an exercise price of $7.58 per share to certain non-employee directors under our 2006 Director Plan.

(4) In July 2006 we granted 85,000 stock units relating to our common stock to certain regional managers under our 2006 Regional Plan.

(5) On October 18, 2006, we granted 765,000 stock options relating to our common stock with an exercise price of $7.83 per share to certain members of our executive management under our 2004 Option Plan.

(6) On April 27, 2007, we granted 50,000 stock options relating to our common stock with an exercise price of $10.26 per share to a member of our executive management under our 2004 Option Plan.

The issuances of securities described in paragraphs (2), (3), (4) and (5) above were made in reliance upon Section 4(2) under the Securities Act in that such issuance did not involve a public offering or under Rule 701 promulgated under the Securities Act, in that they were offered and sold either pursuant to written compensatory plans or pursuant to a written contract relating to compensation, as provided by Rule 701. The issuances of securities described in paragraph (1) above were made in reliance upon Section 4(2) and/or Regulation D promulgated thereunder as transactions not involving any public offering, to purchasers who represented that they were accredited investors as defined under the Securities Act. All share certificates representing the securities issued in such transactions contain appropriate restrictive legends. All of the foregoing shares are deemed restricted securities for the purposes of the Securities Act.

Item 16. Exhibits and Financial Statement Schedules

(a) Exhibits

See the Exhibit Index, which follows the signature pages and is incorporated herein by reference.

(b) Financial Statement Schedules

Schedules not listed above have been omitted because the information to be set forth therein is not material, not applicable or is shown in the financial statements or notes thereto.

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Item 17. Undertakings

(a) The undersigned registrant hereby undertakes to provide to the underwriters at the closing specified in the underwriting agreement, certificates in such denominations and registered in such names as required by the underwriters to permit prompt delivery to each purchaser.

(b) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the registrant pursuant to the foregoing provisions, or otherwise, the registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer, or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Act and will be governed by the final adjudication of such issue.

(c) The undersigned registrant hereby undertakes that:

(1) For purposes of determining any liability under the Securities Act of 1933, the information omitted from the form of prospectus filed as part of this registration statement in reliance upon Rule 430A and contained in a form of prospectus filed by the registrant pursuant to Rule 424(b)(1) or (4) or 497(h) under the Securities Act shall be deemed to be part of this registration statement as of the time it was declared effective.

(2) For the purpose of determining any liability under the Securities Act of 1933, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial *bona fide* offering thereof.

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SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the registrant has duly caused this registration statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the city of Toano, State of Virginia, on October 24, 2007.

Lumber Liquidators, Inc.

By: /s/ JEFFREY W. GRIFFITHS

Jeffrey W. Griffiths

President, Chief Executive Officer and Director

Pursuant to the requirements of the Securities Act of 1933, this registration statement has been signed by the following persons in the capacities and on the dates indicated.

Signature	Title	Date
* **Jeffrey W. Griffiths**	President, Chief Executive Officer and Director	October 24, 2007
* **Daniel E. Terrell**	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	October 24, 2007
* **Thomas D. Sullivan**	Chairman of our Board of Directors	October 24, 2007
* **Richard D. Tadler**	Director	October 24, 2007
* **Martin F. Roper**	Director	October 24, 2007
* **Douglas T. Moore**	Director	October 24, 2007
* **John M. Presley**	Director	October 24, 2007

*By: /s/ E. LIVINGSTON B. HASKELL

E. Livingston B. Haskell, as Attorney-in-Fact

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EXHIBIT INDEX

Exhibit No.	Description
1.01	Form of Underwriting Agreement*
3.01	Form of Restated Certificate of Incorporation
3.02	Form of Restated By-Laws
4.01	Form of Certificate of Common Stock of Lumber Liquidators, Inc.*
5.01	Opinion of Cleary Gottlieb Steen & Hamilton LLP*
10.01	Lumber Liquidators 2006 Equity Plan for Non-Employee Directors[#,**]
10.02	Lumber Liquidators 2004 Stock Option and Grant Plan[#,**]
10.03	Employment Agreement with Jeffrey W. Griffiths[#,**]
10.04	Employment Agreement with H. Franklin Marcus, Jr.[#,**]
10.05	Offer Letter Agreement with Robert M. Morrison[#,**]
10.06	Offer Letter Agreement with Marco Pescara[#,**]
10.07	Form of Non-Qualified Employee Stock Option Agreement[#,**]
10.08	Lease by and between ANO LLC and Lumber Liquidators (relating to Toano facility)**
10.09	Thomas D. Sullivan Stock Option Agreement and Lumber Liquidators, Inc. Guaranty Agreement, and amendment thereto[#,**]
10.10	Lumber Liquidators 2007 Equity Compensation Plan[#],**
10.11	Second Amended and Restated Loan Agreement, dated as of March 23, 2006, by and between Lumber Liquidators, Inc. and Bank of America, N.A. (as amended by the First Amendment to Second Amended and Restated Loan Agreement, dated as of July 31, 2006 and Second Amendment to Second Amended and Restated Loan Agreement, dated as of August 7, 2007) and the related Consolidated, Amended and Restated Term Loan Note, dated as of March 23, 2006, and Amended and Restated Revolving Credit Note, dated as of July 31, 2006
10.12	Revolving Credit Agreement, dated as of August 10, 2007, by and between Lumber Liquidators, Inc. and Bank of America, N.A. and the related Revolving Credit Note, dated as of August 10, 2007.
10.13	Registration Rights Agreement, dated as of December 6, 2004, by and among Lumber Liquidators, Inc. and signatory Investors
23.01	Consent of Cleary Gottlieb Steen & Hamilton LLP (included in Exhibit 5.01)*
23.02	Consent of Ernst & Young LLP
23.03	Consent of Macon F. Brock, Jr.**
24.01	Powers of Attorney**

* To be filed by amendment
** Previously filed
\# Indicates a management contract or a compensatory plan, contract or arrangement