

Lumber Liquidators Holdings, Inc.
Form 10-K
February 19, 2014

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2013
OR

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

For the transition period from _____ to _____

Commission file number: 001-33767

Lumber Liquidators Holdings, Inc.
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or other jurisdiction of incorporation or organization)

27-1310817
(I.R.S. Employer Identification No.)

3000 John Deere Road, Toano, Virginia
(Address of principal executive offices)

23168
(Zip Code)

(757) 259-4280
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$0.001 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

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

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90

days. Yes No

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

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

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

Large Accelerated Filer Accelerated Filer Non-accelerated Filer Smaller Reporting Company
(do not check if a smaller reporting company)

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

At June 30, 2013, the last business day of the Registrant's most recently completed second fiscal quarter, the aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant (based upon the closing sale price of such shares on New York Stock Exchange on June 28, 2013) was approximately \$1.5 billion. Shares of Registrant's common stock held by each executive officer and director and by each entity or person that, to the Registrant's knowledge, owned 10% or more of Registrant's outstanding common stock as of June 30, 2013 have been excluded in that such persons may be deemed to be affiliates of the Registrant. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

Indicate the number of shares outstanding of each of the Registrant's classes of common stock as of February 17, 2014:

Title of Class	Number of Shares
Common Stock, \$0.001 par value	27,477,570

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates certain information by reference from the Registrant's proxy statement for the 2014 annual meeting of stockholders, which will be filed no later than 120 days after the close of the Registrant's fiscal year ended December 31, 2013.

LUMBER LIQUIDATORS HOLDINGS, INC.
ANNUAL REPORT ON FORM 10-K

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENT

This report includes statements of our expectations, intentions, plans and beliefs that constitute “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 and are intended to come within the safe harbor protection provided by those sections. These statements, which involve risks and uncertainties, relate to matters such as sales growth, comparable store net sales, impact of cannibalization, price changes, earnings performance, stock-based compensation expense, margins, return on invested capital, strategic direction, the demand for our products and store openings. We have used words such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “thinks,” “estimates,” “seeks,” “predicts,” “could,” “potential” and other similar terms and phrases, including references to assumptions, in this report to identify forward-looking statements. These forward-looking statements are made based on expectations and beliefs concerning future events affecting us and are subject to uncertainties, risks and factors relating to our operations and business environments, all of which are difficult to predict and many of which are beyond our control, that could cause our actual results to differ materially from those matters expressed or implied by these forward-looking statements. These risks and other factors include those listed in this Item 1A. “Risk Factors,” and elsewhere in this report.

When considering these forward-looking statements, you should keep in mind the cautionary statements in this report and the documents incorporated by reference. New risks and uncertainties arise from time to time, and we cannot predict those events or how they may affect us. There may also be other factors that we cannot anticipate or that are not described in this report that could cause results to differ materially from our expectations. Forward-looking statements speak only as of the date they are made and we assume no obligation to update them after the date of this report as a result of new information, future events or subsequent developments, except as required by the federal securities laws.

References to “we,” “our” and “Lumber Liquidators” generally refers to Lumber Liquidators Holdings, Inc. and its consolidated subsidiaries collectively and, where applicable, individually.

PART I

Item 1. Business.

Overview

Lumber Liquidators Holdings, Inc. and its subsidiaries operated 318 retail stores as of December 31, 2013, with 309 located throughout the United States (“U.S.”) and nine in Ontario, Canada. We operate as a single business segment, with our call center, website and customer service network supporting our retail store operations. 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 assortment of exotic and domestic hardwood species, engineered hardwood, laminate, vinyl plank, bamboo and cork direct to the consumer. We also provide a wide selection of flooring enhancements and accessories, including moldings, noise-reducing underlay, adhesives and flooring tools. Our customer is primarily the homeowner, or a contractor on behalf of a homeowner.

Founded in 1994, Lumber Liquidators is the largest specialty retailer of hardwood flooring in North America. Our initial public offering was in November 2007, and our common stock trades on the New York Stock Exchange under the symbol “LL”. We operate in a holding company structure with Lumber Liquidators Holdings, Inc. serving as our parent company and certain direct and indirect subsidiaries, including Lumber Liquidators, Inc., Lumber Liquidators Services, LLC and Lumber Liquidators Canada Inc., conducting our operations. Lumber Liquidators Holdings, Inc. is a Delaware corporation with headquarters in Toano, Virginia.

Competitive Strengths

We believe our value proposition to the customer is the most complete and the strongest within a highly-fragmented hardwood flooring market. Sourcing directly from the mill provides the foundation for this value proposition, strengthened by our unique store model and the industry expertise of our people.

Our Value Proposition

We compete across our value proposition with retailers ranging from the national home improvement chains to the local flooring store in each market. We believe we have an advantage in comparison to our competition and in aggregate, the most complete solution for the residential consumer in search of hard surface flooring. The components of our value proposition include:

Price. Our retail prices in each merchandise category are generally lower than our competitors. This pricing advantage is usually greatest in the premium products, less at the entry or commodity level. We are able to maintain these prices through our direct sourcing model, including the relationship with the mill, the proprietary products we develop and sell, the singular focus of our supply chain on flooring and our highly profitable store model.

Selection. We offer a broad assortment of flooring in varying widths, species and constructions, including solid and engineered hardwood, laminate, vinyl plank, bamboo and cork. In addition, we offer the customer an extensive selection of moldings, staircases, butcher block and flooring accessories. All of our products are sold under proprietary brands and across a range of price points and quality levels that allow us both to target discrete market segments and to appeal to diverse groups of customers.

Quality. We invest significant resources to design and produce products of the highest quality, including our flagship Bellawood brand. We source directly from mills all over the world, and often are a mill’s most significant relationship. Proprietary brands, supported by these relationships, allow us greater control over product design and production, which we monitor through an expansive network of experienced quality control and assurance professionals positioned both at the mill and at our distribution facilities.

Availability. Our commitment to in-stock inventory levels and our focused supply chain allow our entire assortment to be available to meet our customers' expectations in a manner which we believe is more timely than our competitors. We maintain our best selling products as in-stock inventory at our retail store locations and our distribution facilities maintain inventory levels of our entire assortment for delivery to a store to fulfill a customer order. Each store receives a delivery from one of our distribution centers at least once per week.

People. We position ourselves as hardwood flooring experts and believe our high level of customer service reflects this positioning. Residential customers are generally less familiar with the range of products available and with the purchase process itself. We focus on educating our store associates on product knowledge and engaging the customer in the questions leading to the species and construction of flooring which is best aligned with the type of room, expected wear, climate and site conditions, all while satisfying customer budgetary requirements. Our associates, supported by a call center staff, are trained to understand the unique characteristics and preferred installation method across the broad range of hardwood flooring alternatives.

Our Direct Sourcing Model

Supplier Relationships. We believe sourcing directly from mills enables us to offer a broad assortment of high-quality, proprietary products to our customers at a consistently lower cost than our competitors. We seek to establish strong relationships with mills around the world where the significance of our scale, breadth of assortment and liquidity allow for both higher quality and lower cost. We believe our collaborative relationship enhances the mills' productivity, yield and financial flexibility, such that we access lower net costs than our competitors. We are able to set demanding specifications for product quality and our own quality control and assurance teams are on-site at the mills, coordinating inspection and assurance procedures. We believe the advantages a mill gains by working with us attracts interest from around the world. As a result, we have diversified our purchases across approximately 150 domestic and international mills. We seek long-term, core relationships with mills committed to our demanding product specifications, sustainable supply and regulatory compliance. Therefore, our top 20 suppliers accounted for approximately 64% of our supply purchases in 2013. We are well diversified, however, with our largest mill partner representing approximately 10% of our supply purchases in 2013 and our largest hardwood provider representing approximately 6%.

In 2011, we began a process to continually challenge, and ultimately strengthen, the structure of our sourcing relationships with the best international and domestic mills. Our sourcing initiatives play a key role in maintaining the best combination of quality and value in our product assortment, while reducing product costs. These initiatives, now a continuous and integral part of our sourcing strategy and process, can be segregated into three primary areas:

- o Volume-based discounts and cost sharing for a range of continuing programs, including marketing, product samples and new store openings.
- o Current and potential mill partners' participation in competitive line reviews of specific merchandise categories to evaluate breadth of assortment, quality, logistics and product cost.
- o Direct sourcing with international and domestic mills to control product cost and quality, enhance forecasting and broaden our product assortment.

We are committed to uncompromising integrity across our operations, and quality is a key component of our value proposition. The scale of our purchasing and diversity of products require sustainable forestry. We invest significant time and resources to safeguard quality and comply with regulatory requirements. We discontinue sourcing from suppliers not adhering to our standards. We seek long-term relationships with mills that can provide sustainable and growing supplies of high-quality product.

Our Products and Brands. We offer an extensive assortment of wood flooring under 18 proprietary brand names, led by our flagship, Bellwood. We have invested significant resources developing these national brand names, as well as the Lumber Liquidators name. We expect to continue to invest resources in our advertising and marketing at a percentage of net sales that we believe is greater than our competitors. We believe Lumber Liquidators is now recognized across the U.S. as a destination for high-quality hardwood flooring at low prices, while our Bellwood brand is known as a premium flooring brand within the industry.

Our hardwood flooring products are available in various widths and lengths and generally differentiated in terms of quality and price based on the species, wood grade and durability of finish. Prefinished floors are now the dominant choice for residential customers over unfinished wood planks that have a finish applied after installation. More than 95% of the flooring we sell is prefinished. We also offer a broad assortment of flooring enhancements and installation accessories, including moldings, noise-reducing underlay and tools, that complement our assortment of floor offerings. In total, we offer nearly 350 different flooring product stock-keeping units, however, no single hardwood product represented more than 1% of our sales mix. By major product category, our sales mix was as follows:

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	2013		2012		2011	
	(percentage of net sales)					
Solid and Engineered Hardwood	44	%	48	%	51	%
Laminate, Bamboo, Cork and Vinyl Plank	38	%	36	%	34	%
Moldings and Accessories	18	%	16	%	15	%
Total	100	%	100	%	100	%

Changes in our sales mix are often the primary driver of changes in our sourcing mix for flooring products. We seek the highest quality at the best value, in consideration of where the raw material grows, the amount of labor necessary to construct and produce the unfinished plank or finished board and the transportation costs to our distribution centers or stores. Our sourcing mix of flooring, exclusive of moldings and accessories, by continent was as follows:

Continent	Primary Products Sourced	2013 2012 2011 percentage of flooring sales (excludes moldings and accessories)					
Asia	Laminate, Bamboo, Cork, Vinyl Plank and certain Handscraped and Engineered Hardwood	50	%	43	%	42	%
North America	Solid Domestic Hardwood	40	%	50	%	50	%
South America	Solid Exotic and Engineered Hardwood	7	%	6	%	7	%
Other	Laminate and Exotic Hardwood	3	%	1	%	1	%
	Total	100	%	100	%	100	%

Major product categories include:

Solid and Engineered Hardwood. Our proprietary solid hardwood products are milled from one thick piece of wood, which can be sanded and refinished numerous times, and our proprietary engineered hardwood products are produced by bonding a layer of hardwood to a plywood or high-density fiber board backing. Engineered flooring is designed primarily to be installed in areas where traditional hardwood is not conducive, such as slab construction, basements and areas where moisture may be a factor. 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 sell our solid hardwood products either prefinished or unfinished, and our engineered hardwood products in either glue down or floating application. Our prefinished hardwoods typically carry a wear warranty from 10 to 30 years, and our Bellawood products carry a 100-year, transferable warranty.

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 with a ceramic finish, abrasion-resistant laminate top. Our laminate flooring brands allow for easy-click installation, and some include a pre-glued undersurface, moisture repellent, soundproofing, single-strip format or a handscraped textured finish. Our laminates carry wear warranties ranging from 20 to 30 years.

Bamboo, Cork and Vinyl Plank. Our proprietary bamboo products, harvested from the fast growing bamboo plant, are offered as a prefinished, natural or stained, solid or engineered floor. Our proprietary cork flooring is produced by harvesting the outer bark of the cork oak tree, and it is durable, acoustical and acts as an insulator. Produced from recycled materials, our vinyl plank flooring comes in realistic wood and tile looks, is water-resistant, highly durable and installs with "peel-and-stick" or click-together ease. Our bamboo, cork and vinyl plank flooring products carry wear warranties ranging from 25 to 50 years, and our Bellawood bamboo products carry a 100-year, transferable warranty.

Moldings and Accessories. We offer a wide variety of wood flooring moldings and accessories. Moldings are a required finishing detail to every floor and we sell a complete selection that matches virtually all of our floors or can complement them. We also sell stair treads and risers in both finished and unfinished versions. Accessories include sealers, adhesives and underlayments that are placed between the new floor and the sub-floor, insulating sound and cushioning the floors. In addition, we sell flooring tools, floor cleaning supplies and butcher block kitchen

countertops.

Finishing. In order to control the quality of our Bellawood brand, we maintain a finishing facility in Toano, Virginia. In 2013, we finished more than 26 million square feet of flooring, primarily our Bellawood products. The quality of this process results in Bellawood hardwood products having one of the highest scuff resistant finishes in the industry.

Our current equipment and capacity allow us to effectively finish approximately 83% of the current Bellawood demand. To supplement the balance needed, we certify and continually monitor the finishing processes of certain mills in both North America and South America. In 2014 and over the next several years, we intend to invest in the equipment and processes needed to significantly enhance our capacity to finish Bellawood products in our Toano facility.

Supply Chain. We are committed to our complete product assortment being available to meet our customers' expectations more timely than our competitors. We have a strategic, multi-year initiative to optimize our supply chain, supporting our continued store base expansion while focused on continuous improvement in the efficiency and effectiveness of our supply chain operations.

In 2013, we operated distribution facilities in Hampton Roads and Toano, Virginia, and a small facility in Toronto, Canada. We also lease the services of a third party consolidation center in China to break bulk shipments from mills into quantities and assortments that can be sent directly to our store locations. On average, each store location has approximately 4,400 to 6,000 square feet of warehouse space stocked with a combination of customer-specific inventory waiting to be picked up or delivered and inventory levels of certain products we believe the customer expects to be immediately available. Where possible, we work with our mills to ship certain products directly to our stores, or in rare cases, to our customers.

Our product is generally transported boxed and palletized, and the weight of our product generally increases our supply chain costs. Our transportation costs are significant, representing 8.7% of net sales in 2013, and are impacted by international container rates, customs and duty charges, and domestic fuel costs. Our supply chain initiatives seek the lowest rates, reductions in the number of miles traveled and the most efficient means to minimize the total cost per mile. Transportation costs include:

- international and domestic inbound transportation to either our distribution centers or stores;
- transportation charges from our distribution centers to our stores;
- transportation charges between stores; and
- third party delivery services from our stores to our customers.

In August 2013, we reached agreements to strengthen the long-term structure of our supply chain through the consolidation and expansion of our distribution facilities. We entered into a lease for a 500,000 square foot distribution center in Pomona, California and agreed to purchase 110 acres of undeveloped land in Henrico County, Virginia where we are constructing a 1.0 million square foot distribution center.

We expect the West Coast facility to be fully operational in the first quarter of 2014, providing customers shopping in our stores west of Texas even greater flexibility in the timing of their flooring projects. The new facility in Henrico County, Virginia is expected to be fully operational late in the fourth quarter of 2014 and will consolidate the operations currently in 750,000 leased square feet across four separate buildings in the Hampton Roads area of Virginia. While immediately providing greater efficiency, this new facility will also provide significant flexibility for store base expansion.

Our Unique Store Model

Our stores are approximately 6,000 to 7,000 square feet, which includes a showroom format designed to emphasize our products and a small warehouse. We adapt a range of existing buildings to our format, from free-standing to strip center to small shopping center. Flooring generally is a considered, well-researched purchase, and we believe our value proposition makes us a destination location. Therefore, we are able to seek locations with generally lower rent than those retail concepts requiring high traffic or impulse purchases. We enter into short leases, generally for a base term of five years, with renewal options to maximize our real estate flexibility. We believe that our store design and locations reinforce our customers' belief that they get a good deal when they buy from us.

Through 2011, we targeted locations that placed high significance on visibility to passing traffic and easy access from major highways. Thereafter, we have sought locations with certain retail synergies, including home improvement. Through 2012, we employed various showroom designs with a target of 1,000 to 1,200 square feet and allocated the remaining space to warehousing. In January 2013, we began using the initial design of an expanded store showroom to enhance the shopping experience for our customers. We refer to this showroom, coupled with an improved store warehouse design, as our "store of the future." The store of the future retains our targeted location size but expands the

average showroom to a structured design of approximately 1,600 square feet. Each of our 30 new stores opened in 2013 utilized the store of the future design. In addition, through December 31, 2013, we had remodeled 22 existing stores to the new format, including six stores relocated within the primary trade area. We expect all of our new stores and all of our existing stores that we remodel or relocate to will be in this format.

Our store showrooms have wall racks holding one-foot by two-foot display boards of our flooring products, presented within color palate and in a good-better-best format, and larger sample squares serving as the showroom floor. The showroom also displays an expanded selection of flooring enhancements and accessories to install, complement and maintain a customer's new floor.

A typical store staff consists of a manager and two to three associates, with a compensation structure that generally weights sales-driven commission bonuses over relatively low base salaries. The store manager is responsible both for store operations and for overseeing our customers' shopping experience. A store's warehouse is stocked with a combination of that store's most popular products and high-volume items, as well as customer-specific inventory waiting to be picked up or delivered. In-store merchandise inventory levels are impacted by sales volume, distance from a distribution center, sales mix and warehouse size. At December 31, 2013, in-store inventory ranged as high as \$900,000 per store, but averaged approximately \$400,000 per store. By generally requiring a 50% deposit when an order is placed for product not taken home that day, we reduce store-level working capital requirements.

Our People as Flooring Experts

A flooring purchase is generally a large-ticket, discretionary purchase that most residential homeowners purchase infrequently. Few home improvements, however, have as much consequence to the ambience of a room as the flooring. A flooring purchase is often well-researched, but can be highlighted by emotion. A large segment of residential homeowners are in need of a trusted expert, whether as a guide through a range of flooring alternatives and services or as a resource to a do-it-yourself (“DIY”) customer. We train and position our store management and associates to establish these individual customer relationships, which often last beyond the current purchase to subsequent purchases for additional rooms in the existing house or even to remodeling of a new home.

In conjunction with our Best People initiative, we place an emphasis on identifying, hiring and empowering top performing employees who share a passion for our business philosophy. Many of our store managers have previous experience with the home improvement, retail flooring or flooring installation industries. We provide continuous training for our store associates, from topic-specific modules offered on our intranet to participation in our Lumber Liquidators University (“LLU”) program. LLU is an annual training event for all of our regional and store managers that focuses on enhanced selling techniques, in-depth product training and strategic discussions with senior executives.

We divide our U.S. stores into three primary geographic regions, each with a vice-president of sales, and further segregate stores into regions with 10 to 15 stores overseen by a regional manager. At least one store in each region is designated as a training store, adding to the skills of existing associates, sharing best practices and developing future store managers. Our hours of operation are generally less than traditional retail and sales are less weighted to weekends. Combined with a low number of associates supervised per location and average annual compensation of \$80,000 to \$90,000, we believe our store manager position is valued in retail and our turnover is low.

Sales Approach

We seek to appeal to customers who desire a high-quality product at an attractive value. We sell our products principally to existing homeowners who we believe represent over 90% of our customer count. Most of our other sales are to contractors, who are primarily small businesses that are either building a limited number of new homes or have been hired by a residential owner to put in a new floor.

Historically, our customers are in their mid-30’s or older, are well-educated and have income levels above the average domestic household. We have found that homeowners prefer an assortment with a range of characteristics, including appearance and durability, ease of installation, renewability of resources, and specific aspects of engineered, vinyl plank and laminate flooring. Our research indicates that our customers will choose to replace their flooring primarily after they have lived in the home for a certain number of years, when a life event occurs such as a change in household members, and prior to or shortly after moving into a new home. According to Catalina Research, Inc. (“Catalina”), approximately 28% of buyers of an existing home undertake some type of flooring replacement project in the first year of ownership.

Our primary focus has been on customers who are passionate about their flooring purchase and who often define themselves as DIY. In recent years, we believe our value proposition has reached, and resonated with, both the DIY customer and a customer considered more “casual.” The casual consumer generally has less knowledge of the range of hard surface flooring products available or the purchase process itself, including the key questions needed for the best flooring solution. In comparison to the DIY customer, this customer generally requires a broader range of assistance from our sales associates and traditionally selects additional services such as delivery and installation.

We compete for the DIY and more casual customers in a highly fragmented marketplace, where we believe no one retailer has captured more than a 15% share of the market for hardwood flooring. We believe the majority of the

market consists of local one-store flooring retailers, small chains of stores that may specialize in one or two flooring categories and a limited number of regional chains. While these independent retailers once numbered over 13,000 and suffered during the downturn in residential home improvement, Catalina estimates there are still 9,000 specialty floor coverings stores.

We also compete against the national home improvement warehouse chains, including Home Depot and Lowe's, which together have over 4,000 store locations. Catalina estimates that Lumber Liquidators, Home Depot and Lowe's combined represent approximately one-third of hardwood flooring retail sales. We believe we have a greater market share in the products we sell, and further believe our product categories represent less than 2% of sales at an average Home Depot or Lowe's store.

We are the largest specialty retailer of hardwood flooring in North America, and we capture market share from competitors ranging from the local store to the national home improvement chain by offering the strongest, most complete value proposition, aggressively broadening the reach and frequency of our marketing and advertising, and delivering a complete flooring solution with expertise and continuing service.

Marketing and Advertising

Reach and Frequency. Our marketing and advertising strategy includes a focus on broadening the reach and frequency of our message to increase the recognition of our value proposition and ultimately the number of customers served. We utilize a mix of traditional and new media, direct mail and financing offers to emphasize product credibility, value, brand awareness, customer education and direct selling.

We increase brand awareness in a variety of ways, including celebrity endorsements and product placement opportunities. We have on-going relationships with respected, well-known home improvement celebrities Bob Vila and Ty Pennington. Bob Vila, in particular, has been associated specifically with our Bellawood brand for several years.

To increase brand awareness, we conduct ad campaigns on both a national and local level using both traditional and new media. We work with shows such as HGTV's "Dream Home Sweepstakes" and "This Old House", 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. In addition, we use targeted television advertising across both cable and national networks. We engage in sports marketing by participating in opportunities with, among others, Major League Baseball and National Basketball Association teams. On the Internet, our advertising efforts include the use of banner advertising, sponsoring links on well-known search engines, having storefronts with large e-tailers and having a large network of online affiliate partners. We also utilize local and national radio, primarily for promotional messaging.

Our direct mail strategy focuses on regular contact with our customers and the targeting of prospective purchasers. We have a healthy and growing database that we utilize to drive our direct mail and overall marketing strategies. We distribute our catalogs, as well as other direct mailings, to key consumer and commercial segments around specific store locations. Copies of our catalogs can also be obtained through our stores, our call center and our website. In addition, we utilize direct mail for call-to-action promotions. We expect to continue expanding our direct mailing efforts to prospective customers in markets where we have stores.

Financing. We offer our residential customers a financing alternative through a proprietary credit card, the Lumber Liquidators credit card, underwritten by a third party financial institution at no recourse to us. This program serves the dual function of providing financial flexibility to our customers and offering us promotional opportunities featuring deferred interest, which we often combine with product promotions. Our customers may also use their Lumber Liquidators credit card to tender installation services provided by our third party service provider.

We offer our commercial customers a financing alternative through the Lumber Liquidators Commercial Credit Program, A Credit Line for Pros. This program is underwritten by a third party financial institution, generally at no recourse to us. The commercial credit program also provides our professional customers a range of additional services that we believe add efficiency to their businesses.

Services

We have an integrated multi-channel sales model that enables our stores, call center, website and catalogs to work together in a coordinated manner. We believe that due to the average size of the sale and the general infrequency of a hardwood flooring purchase, many of our customers conduct extensive research using multiple channels before making a purchase decision. Our research indicates that the average length for a hardwood flooring purchase, from initial interest to sale, is approximately 100 days.

As flooring experts, we strive to support all stages of the purchase cycle. Our objective is to help the consumer throughout the process from aspiration to installation advice, whether in our store or in their home. Our sales strategy emphasizes customer service by providing superior, convenient, educational tools for our customers to learn about our products and the installation process. Our website contains a broad range of information regarding our floors and accessories. Visitors to our website can search through a comprehensive knowledge base of tools on wood flooring, including browsing product reviews, frequently asked questions and an extensive "before and after" gallery from previous customers, as well as research detailed product information and how-to videos that explain the installation process. A consumer also has the ability to chat live with a flooring expert for questions about a flooring purchase or installation, either online or over the phone. We have also developed several new responsive mobile, tablet and website functions to assist consumers with their flooring choice. For example, our Designer Toolbox brings together several functions such as a virtual room designer and Color Match, which allows customers to match their floor to a specific color, cabinet, furniture or competitive option.

Flooring samples of all the products we offer are available in our stores, and can be ordered through our call center and website. In addition, our iPhone and iPad app, The Floor Finder, gives consumers access to approximately 200

digital samples as well as a variety of tools designed to facilitate flooring purchase decisions, including visualizing any floor in their own home. The app also gives consumers flooring specifications, such as hardness and installation information. We engage and interact in social media in order to connect to our consumers in the most convenient manner possible as well as build relationships with our satisfied customers. We have an active presence on Facebook, Pinterest, YouTube and three unique Twitter accounts.

We strive to use our various sales channels to make our customers' transactions easy and efficient. Customers can purchase our complete assortment of products in our stores, or through our call center, website, a smartphone or a tablet. The prices available on our website and from our call center are the same as the prices in our stores. Once an order is placed, customers may have their purchases delivered or pick them up at a nearby store location. Our average sale was approximately \$1,705 in 2013, and generally represents one or two rooms of flooring. 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 goal is to provide our customers with everything needed to complete their flooring project to remove the existing floor, install the new floor with complementary moldings and accessories, and finally, maintain the floor for its lifetime.

We are committed to responding timely to all of our potential and existing customers. Our call center is staffed by flooring experts cross-trained in sales, customer service and product support. In addition to receiving telephone calls, our call center associates chat online with visitors to our website, responds to emails from our customers and engages in telemarketing activities. Customers can contact our call center to place an order, to make an inquiry or to order a catalog.

Store to Customer Delivery. Once an order is placed, a customer chooses to pick up at a nearby store location or have their purchases delivered. We engage third parties to deliver our products from the store to an address designated by the customer. The cost of the delivery varies based on weight and distance, and we pass our actual cost onto the customer with a small markup to cover administration. In 2013, actual third party delivery charges included in cost of sales were 91% of the delivery revenue included in net sales. As our value propositions has resonated with a more casual customer, we have seen greater use of delivery, to approximately 14% of our customers in 2013 compared to approximately 11% in 2012. We believe our attachment of delivery services will continue to increase as we attract more casual consumers.

Installation. In each of our stores, we provide fully-insured and licensed professional installation services to measure and install flooring at competitive prices. Through 2012, these services were managed through a national arrangement with a third party. In 2013, we began testing structural alternatives to the current installation arrangement. These alternatives focus on our own associates performing certain customer-facing services and managing the actual installation services provided by third party, fully-insured and licensed professionals in each market. Customer-facing services are consultative in nature, providing the customer with a primary contact from initial in-home measurement to final approval of the installed floor.

Under the arrangement with the third party, we receive certain reimbursements based upon our customers' use of their services, with which we offset certain other expenses. Service revenue for installation transactions we control are included in net sales, with the corresponding costs in cost of sales. The gross margin on these transactions was less than the company average. In both 2013 and 2012, less than 8% of our customers chose installation services. We believe our greater interaction with the customer and greater control over the third party services provided will ultimately result in higher utilization by the customer.

Market

According to the July 2013 Floor Coverings Industry report and quarterly updates from Catalina, the hardwood flooring market represents approximately 11% of the overall U.S. floor coverings market, which includes carpet and area rugs, solid and engineered hardwood, softwood and bamboo flooring, ceramic and stone floor and wall tile, resilient sheet and floor tile, and laminate flooring. Due to improvements in the quality and construction of certain products, ease of installation and lower average retail price points, hardwood flooring's share of the overall U.S. floor coverings market continues to increase, primarily by taking share from soft surface flooring. Using Catalina estimates as a basis, we believe the 2013 retail value of the U.S. hardwood and laminate flooring markets were approximately \$4.2 billion and \$1.8 billion, respectively. Our share of the combined market was approximately 10.2% considering these products were approximately 64% of our sales mix in 2013.

The residential replacement wood flooring market is dependent on home-related, large-ticket discretionary spending, which is itself influenced by a number of complex economic and demographic factors that may vary locally, regionally and nationally. We believe this market is impacted by, among other things, home remodeling activity, employment levels, housing turnover, home prices, new housing starts, consumer confidence, borrowing rates, credit availability and the general health of consumer discretionary spending. Overall, a number of these factors generally improved during both 2012 and 2013. However, many remain at levels lower than historical averages. We expect continued strengthening over time, but marked by periodic volatility when our customer is likely to be cautious and price-sensitive.

Catalina projects the hardwood flooring market will average annual growth of 5.0% per year through 2018, and perhaps greater, subject to the pace of macroeconomic recovery. We believe floor covering sales lag single-family existing homes sales by approximately one year. As such, we believe we are well-positioned to benefit from an improving housing market in the coming years. We continue to believe that the longer term trends for our market remain favorable, including customer perception of hardwood flooring as an attractive alternative to other floor coverings, the evolution of the hardwood flooring market, overall home improvement spending and certain demographic trends.

Employees

As of December 31, 2013, we had 1,750 employees, 95% of whom were full-time and none of whom were represented by a union. Of these employees, 70% work in our stores, 18% work in corporate store support infrastructure or similar functions (including our call center employees) and 12% work either on our finishing line or in our distribution centers. We believe that we have good relations with our employees.

Seasonality and Quarterly Results

Our quarterly results of operations fluctuate depending on the timing of our advertising expenses and the timing of, and income contributed by, our new stores. 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 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.

Intellectual Property and Trademarks

We have a number of marks registered in the United States, including Lumber Liquidators®, Bellawood®, 1-800-HARDWOOD®, 1-800-FLOORING®, Dura-Wood®, Quickclic®, Virginia Mill Works Co. Hand Scraped and Distressed Floors®, Morning Star Bamboo Flooring®, Dream Home Laminate Floors®, Builder's Pride®, Schön Engineered Floors®, Casa de Colour Collection® and other product line names. We have also registered certain marks in jurisdictions outside the United States, including the European Union, Canada, China, Australia and Japan. We regard our intellectual property as having significant value and these names are an important factor in the marketing of our brands. Accordingly, we take steps intended to protect our intellectual property including, where necessary, the filing of lawsuits and administrative actions to enforce our rights. 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, provincial, state and local government regulations in the jurisdictions in which we operate, including laws and regulations relating to our relationships with our employees, public health and safety, zoning and fire codes. We operate each of our stores, offices, finishing facility and distribution centers in accordance with standards and procedures designed to comply with applicable laws, codes and regulations.

Our operations and properties are also subject to federal, provincial, 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 cleanup of contaminated properties, including off-site disposal locations. We do not incur significant costs complying with these laws and regulations. However, we could be subject to material costs, liabilities or claims relating to compliance in the future, especially in the event of changes in existing laws and regulations or in their interpretation.

Our suppliers are subject to the laws and regulations of their home countries, including in particular laws regulating labor, forestry and the environment. We consult with our suppliers, as appropriate, to ensure that they are in compliance with their applicable home country laws. We also support social and environmental responsibility among our supplier community and our suppliers agree to comply with our expectations concerning environmental, labor and health and safety matters. Those expectations include representations and warranties that our suppliers comply with the laws, rules and regulations of the countries in which they operate.

Products that we import into the United States and Canada are subject to laws and regulations imposed in conjunction with such importation, including those issued and/or enforced by U.S. Customs and Border Protection and the Canadian Border Services Agency. In addition, certain of our products are subject to laws and regulations relating to the importation, acquisition or sale of illegally harvested plants and plant products and the emissions of hazardous materials. We work closely with our suppliers in order to comply with the applicable laws and regulations in these areas.

We believe that we currently conduct, and in the past have conducted, our activities and operations in substantial compliance with applicable laws and regulations relating to the environment and protection of natural resources. However, there can be no assurance that such laws will not become more stringent in the future or that we will not incur additional costs in the future in order to comply with such laws.

Available Information

We maintain a website at www.lumberliquidators.com. The information on or available through our website is not, and should not be considered, a part of this report. You may access our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, as well as other reports relating to us

that are filed with or furnished to the Securities and Exchange Commission (“SEC”) free of charge at our website as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. In addition, you may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site, www.sec.gov, which contains reports, proxy and information statements, and other information that we file electronically with the SEC.

Item 1A. Risk Factors.

The risks described below could materially and adversely affect our business, results of operations, financial condition and cash flows. These risks are not the only risks that we face. Our business operations could also be affected by additional factors that apply to all companies operating in the U.S. and globally, as well as other risks that are not presently known to us or that we currently consider to be immaterial.

Risks Related to Economic Factors and Our Industry

Changes in economic conditions may adversely impact demand for our products, reduce access to credit and cause our customers and others with whom we do business to suffer financial hardship, all of which could adversely impact our business, results of operations and financial condition.

Our business, financial condition and results of operations have and may continue to be affected by various economic factors. Changes in the current economic environment and uncertainty about the future coul