

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 27, 2018

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 001-38070

Floor & Decor Holdings, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of Incorporation or Organization)

27-3730271
(I.R.S. Employer Identification No.)

2233 Lake Park Drive Smyrna, Georgia
(Address of Principal Executive Offices)

30080
(Zip Code)

Registrant's telephone number, including area code (404) 471-1634

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

Table with 2 columns: Title of each class, Name of each exchange on which registered. Row 1: Class A Common Stock \$0.001 par value 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 [x] No [ ]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes [ ] No [x]

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

Yes [x] No [ ]

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files).

Yes [x] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§299.405 of this chapter) is not contained herein, and will not be contained, to the best of the 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. [x]

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

Large accelerated filer [x] Accelerated filer [ ]
Non-accelerated filer [ ] Smaller reporting company [ ]
Emerging growth company [ ]

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. [ ]

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

The aggregate market value of the Registrant's Common Stock held by non-affiliates as of June 28, 2018 was \$ 2.3 billion. There were 97,727,273 shares of Common Stock outstanding as of as of February 20, 2019.

Documents Incorporated by Reference:

Portions of the Registrant's proxy statement for the Annual Meeting of Shareholders to be filed pursuant to Regulation 14A of the Exchange Act on or before April 26, 2019, are incorporated by reference into Part III of this Form 10-K.

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## PART I

### FORWARD LOOKING STATEMENTS .

The discussion in this Annual Report on Form 10-K (this “Annual Report”), including under Item 1A, “Risk Factors” of Part I and Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of Part II, contains forward-looking statements. All statements other than statements of historical fact contained in this Annual Report, including statements regarding our future operating results and financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. These statements involve known and unknown risks, uncertainties and other important factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Forward-looking statements are based on management’s current expectations and assumptions regarding the Company’s business, the economy and other future conditions, including the impact of natural disasters on sales. In some cases, you can identify forward-looking statements by terms such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “seeks,” “intends,” “target,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “budget,” “potential” or “continue” or the negative of these terms or other similar expressions.

The forward-looking statements contained in this Annual Report are only predictions. Although we believe that the expectations reflected in the forward-looking statements in this Annual Report are reasonable, we cannot guarantee future events, results, performance or achievements. A number of important factors could cause actual results to differ materially from those indicated by the forward-looking statements in this Annual Report, including, without limitation, those factors described in Item 1A, “Risk Factors” of Part I and Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of Part II. Some of the key factors that could cause actual results to differ from our expectations include the following:

- an overall decline in the health of the economy, the hard surface flooring industry, consumer spending and the housing market;
- any disruption in our distribution capabilities resulting from our inability to operate our distribution centers going forward;
- competition from other stores and internet-based competition;
- our failure to execute our business strategy effectively and deliver value to our customers;
- our inability to manage our growth;
- our inability to manage costs and risks relating to new store openings;
- our dependence on foreign imports for the products we sell, which may include the impact of tariffs;
- our inability to find, train and retain key personnel;
- violations of laws and regulations applicable to us or our suppliers;
- our failure to adequately protect against security breaches involving our information technology systems and customer information;
- our failure to successfully anticipate consumer preferences and demand;
- our inability to find available locations for our stores or our store support center on terms acceptable to us;
- our inability to obtain merchandise on a timely basis at prices acceptable to us;
- suppliers may sell similar or identical products to our competitors;
- our inability to maintain sufficient levels of cash flow to meet growth expectations;
- our inability to manage our inventory obsolescence, shrinkage and damage;
- fluctuations in material and energy costs;
- our vulnerability to natural disasters and other unexpected events; and

· restrictions imposed by our indebtedness on our current and future operations.

Because forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified, you should not rely on these forward-looking statements as predictions of future events. The forward-looking statements contained in this Annual Report speak only as of the date hereof. New risks and uncertainties arise over time, and it is not possible for us to predict those events or how they may affect us. If a change to the events and circumstances reflected in our forward-looking statements occurs, our business, financial condition and operating results may vary materially from those expressed in our forward-looking statements. Except as required by applicable law, we do not plan to publicly update or revise any forward-looking statements contained herein, whether as a result of any new information, future events or otherwise.

**ITEM 1. BUSINESS .**

Except where the context suggests otherwise, the terms “Floor & Decor Holdings, Inc.,” “Floor & Decor,” the “Company,” “we,” “us,” and “our” refer to Floor & Decor Holdings, Inc., a Delaware corporation, together with its consolidated subsidiaries.

Our fiscal year is the 52 or 53 week period ending on the Thursday preceding December 31. The following discussion contains references to fiscal 2014, fiscal 2015, fiscal 2016, fiscal 2017, fiscal 2018, fiscal 2019, and fiscal 2020, which represent our fiscal years ended or ending, as applicable, December 25, 2014, December 29, 2016, December 28, 2017, December 27, 2018, and December 26, 2019, all of which are 52 week periods, and our fiscal years ended December 31, 2015, and December 31, 2020, which are 53 week periods.

**Our Company**

Founded in 2000, Floor & Decor is a high-growth, differentiated, multi-channel specialty retailer of hard surface flooring and related accessories with 100 warehouse-format stores across 28 states. We believe that we offer the industry’s broadest in-stock assortment of tile, wood, laminate, vinyl, and natural stone flooring along with decorative and installation accessories at everyday low prices positioning us as the one-stop destination for our customers’ entire hard surface flooring needs. We appeal to a variety of customers, including professional installers and commercial businesses (“Pro”), Do It Yourself customers (“DIY”) and customers who buy the products for professional installation (“Buy it Yourself” or “BIY”). Our Pro customers are loyal, shop often and help promote our brand. The combination of our category and product breadth, low prices, in-stock inventory in project-ready quantities, proprietary credit offerings, free storage options and dedicated customer service positions us to gain share in the attractive Pro customer segment. We believe our DIY customers spend significant time planning their projects while conducting extensive research in advance. We provide our customers with the education and inspiration they need before making a purchase through our differentiated online and in-store experience.

Our warehouse-format stores, which average approximately 75,000 square feet, are typically larger than any of our specialty retail flooring competitors’ stores. Other large format home improvement retailers only allocate a small percentage of their floor space to hard surface flooring and accessories. When our customers walk into a Floor & Decor store for the first time, we believe they are amazed by our visual presentation, our store size, our everyday low prices and the breadth and depth of our merchandise. We believe that our inspiring design centers, creative and informative visual merchandising, and accessible price points greatly enhance our customers’ experience. Our stores are easy to navigate and designed to interactively showcase the wide array of designs and product styles a customer can create with our flooring and decorative accessories. We engage our customers both through our trained store associates and designers who can assist in narrowing choices and making the process of home renovation easier, as well as our staff dedicated to serving Pro customers. By carrying a deep level of in-stock hard surface flooring inventory and wide range of tools and accessories, we seek to offer our customers immediate availability on everything they need to complete their entire flooring or remodeling project. In addition to our stores, our website *FloorandDecor.com* showcases our products, offers informational training and design ideas and has our products available for sale, which a customer can pick up in-store or have delivered. Our ability to purchase directly from manufacturers through our direct sourcing model enables us to be fast to market with a balanced assortment of bestseller and unique, hard to find items that are the latest trend-right products. We believe these factors create a differentiated value proposition for Floor & Decor and drive customer loyalty with our Pro, DIY and BIY hard surface flooring customers in our markets, as evidenced by our track record of consistent double digit comparable store sales growth, which has averaged 14.9% over the last five years. Based on these characteristics, we believe Floor & Decor is redefining and expanding the addressable market size of the hard surface flooring category and that we have an opportunity to significantly expand our store base to approximately 400 stores nationwide within the next 10-15 years, as described in more detail below.

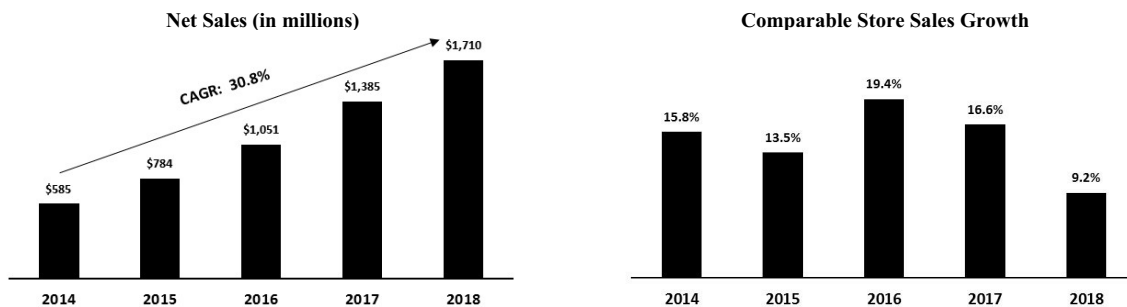
Our Company was founded in 2000 by our Vice Chairman Vincent West, who opened the first Floor & Decor store in Atlanta, Georgia, with the vision of being the low-price leader for hard surface flooring. As we have grown, we have implemented a customer-focused and decentralized approach to managing our business. We provide our store leadership and regional operating teams with regular training and sophisticated information technology systems. We also train and incentivize our store associates to deliver a superior experience to our customers. Taken together, these elements create a customer-centric culture that helps us achieve our operational and financial goals.

Over the last several years, we have invested significant resources across our business and infrastructure to support innovation and growth. We believe that these investments will continue to strengthen our customer value proposition and further differentiate Floor & Decor from our competition, positioning us for continued market share gains. We have made significant

investments in product innovation across all categories, improving our assortment and seeking to provide more value to our Pro, DIY and BIY customers. We have also invested in technology and personnel to support our stores. We believe that our investments in our business will continue to improve our customer value proposition, differentiating us and strengthening our competitive advantage.

We believe our strong financial results are a reflection of our consistent and disciplined culture of innovation and reinvestment, creating a differentiated business model in the hard surface flooring category, as evidenced by the following:

- ten years of comparable store sales growth averaging 14.8% per year (and averaging 14.9% per year for fiscal 2014 to fiscal 2018), with a 9.2% increase in fiscal 2018 compared to 16.6% for fiscal 2017
- store base expansion from 47 warehouse-format stores at the end of fiscal 2014 to 100 warehouse-format stores at the end of fiscal 2018, representing a compound annual growth rate (“CAGR”) of 20.8%; we added 17 warehouse-format stores during fiscal 2018, which was a 20.5% growth in units compared to fiscal 2017;
- total net sales growth from \$584.6 million to \$1.71 billion from fiscal 2014 to fiscal 2018, representing a CAGR of 30.8%;
- net income growth from \$15.1 million to \$116.2 million from fiscal 2014 to fiscal 2018, representing a CAGR of 66.6%;
- Adjusted EBITDA growth from \$51.2 million to \$191.9 million from fiscal 2014 to fiscal 2018, representing a CAGR of 39.1%, which includes significant investments in our sourcing and distribution network, integrated IT systems and corporate overhead to support our future growth. Adjusted EBITDA was \$191.9 million for fiscal 2018, an increase of 20.9% over fiscal 2017. Adjusted EBITDA is a non-GAAP (as defined below) financial measure. For a reconciliation of net income to Adjusted EBITDA, see Item 6 “Selected Financial Data.”



### Our Competitive Strengths

We believe our strengths, described below, set us apart from our competitors and are the key drivers of our success.

*Unparalleled Customer Value Proposition.* Our customer value proposition is a critical driver of our business. The key components include:

- *Differentiated Assortment Across a Wide Variety of Hard Surface Flooring Categories.* Our stores are generally larger than those of our specialty retail flooring competitors, and we allocate substantially more square footage to hard surface flooring and accessories than other large format home improvement retailers. We believe we have the most comprehensive in-stock, trend-right product assortment in the industry within our categories with on average approximately 3,800 stock keeping units (“SKUs”) in each store which, based on our market experience, is a far greater in-stock offering than any other flooring retailer. Additionally, we customize our product assortment at the store level for

the regional preferences of each market. We have an ongoing product line review process across all categories that allows us to identify and interpret emerging trends in hard surface flooring. We work with our suppliers to quickly introduce new products and styles in our stores. We appeal to a wide range of customers through our “good/better/best” merchandise selection, as well as through our broad range of product styles from classic to modern, as well as new trend-right products. We consistently innovate with proprietary brands and products that appeal to certain customers with over 50 proprietary brands, including AquaGuard®, DuraLux®, and NuCore®.

· *Low Prices.* We provide everyday low prices in the retail hard surface flooring market. Our merchandising and individual store teams competitively shop each market so that we can offer our flooring products and related accessories at low prices. We also work with our vendors to identify and create new, affordable products in categories traditionally considered high-end to further democratize hard surface flooring by providing a greater number of options to a larger customer base. We believe we are unique in our industry in employing an “everyday low price” strategy, where we strive to offer our products at consistently everyday low prices throughout the year instead of engaging in frequent promotional activities. Our ability to provide these low prices is supported by our direct-sourcing model, which strives to eliminate third-party intermediaries and shortens time to market. We believe this strategy creates trust with our Pro, DIY and BIY customers because they consistently receive low prices at Floor & Decor without having to wait for a sale or negotiate to obtain the lowest price.

· *One-Stop Project Destination with Immediate Availability.* We carry an extensive range of products, including flooring and decorative accessories, as well as installation accessories such as thin set, underlayment, grout and tools, to fulfill a customer’s entire flooring project. Our large in-stock assortment, including decorative and installation accessories, differentiates us from our competitors. Our stores stock job-size quantities to immediately fulfill a customer’s entire flooring project. In the instance where a product is not available in the store, our three regional distribution centers and neighboring stores can quickly ship the product to meet a customer’s needs. On average, each warehouse-format store carries approximately 3,800 SKUs, which equates to 1.3 million square feet of flooring products or \$2.5 million of inventory at cost. Customers also have access to all of our inventory for in-store pick up or delivery through *FloorandDecor.com*.

*Unique and Inspiring Shopping Environment.* Our stores average approximately 75,000 square feet and are typically designed with warehouse features including high ceilings, clear signage, bright lighting and industrial racking and are staffed with knowledgeable store associates. We offer an easy-to-navigate store layout with clear lines of sight and departments organized by our major product categories of tile, wood, laminate, vinyl, natural stone, decorative accessories and installation accessories. We believe our unique signage, which clearly displays individual product features and benefits, improves the ease of shopping and facilitates customer decision making. We use merchandise displays and point of sale marketing throughout our stores to highlight product features, benefits and design elements. These features educate and enable customers to visualize how the product would look in their homes or businesses. Furthermore, we encourage customers to interact with our merchandise, to experiment with potential designs and to see the actual product they will purchase, an experience that is not possible in flooring stores that do not carry in-stock inventory in project-ready quantities. The majority of our stores have design centers that showcase project ideas to further inspire our customers, and we employ experienced designers in all of our stores to provide free design consulting. Additionally, we provide a robust online experience for potential customers on *FloorandDecor.com*. For our DIY customers, we also offer weekly “how-to” installation classes on Saturdays. We believe inspiring and educating customers within our stores and on our website provides us with a significant competitive advantage in serving our customers.

*Extensive Service Offerings to Enhance the Pro Customer Experience.* Our focus on meeting the unique needs of the Pro customer, and by extension the BIY customer, drives our estimated sales mix of approximately 60% Pro and BIY customers, which we believe represents a higher percentage than our competitors. We provide an efficient one-stop shopping experience for our Pro customers, offering low prices on a broad selection of high-quality flooring products, deep inventory levels to support immediate availability of our products, modest financial credit, free storage for purchased inventory, the convenience of early store hours and, in most stores, separate entrances for merchandise pick-up. Additionally, each store has a dedicated Pro sales force with technology to service our Pro customer more efficiently, and we have rolled out Pro Zones, which are areas offering a variety of services to Pro customers, in a majority of our stores. We believe by serving the needs of Pro customers, we drive repeat and high-ticket purchases, customer referrals and brand awareness from this attractive and loyal customer segment.

*Decentralized Culture with an Experienced Store-Level Team and Emphasis on Training.* We have a decentralized culture that empowers managers at the store and regional levels to make key decisions to maximize the customer experience. Our store managers, who carry the title Chief Executive Merchant, have significant flexibility to customize product mix, pricing, marketing, merchandising, visual displays and other elements in consultation with their regional leaders. We tailor the merchandising assortment for each of our stores for local market preferences, which we believe differentiates us from our national competitors that tend to have standard assortments across markets. Throughout the year, we train all of our employees on a variety of topics, including product knowledge, sales strategies, leadership and store operations. Our store managers and store department managers are an integral part of our company, and many have over 15 years of relevant industry experience in retail. We have made important investments in the training and development of our people, including the creation of a full time training department. Approximately 73% of our new store management positions are filled through internal promotions, including 92% of our Chief Executive Merchants. We also have incentive compensation programs for all employees, regardless of position or title. We train prospective store managers at our Floor & Decor University, which is part of an extensive training program. Once a year, we hold a four day training session with our senior management, regional directors and store managers, where we focus on the upcoming year's strategic priorities to keep our entire business aligned. We believe our decentralized culture and coordinated training foster an organization aligned around providing a superior customer experience, ultimately contributing to higher net sales and profitability.

*Sophisticated, Global Supply Chain.* Our merchandising team has developed direct sourcing relationships with manufacturers and quarries in over 21 countries. Through these relationships, we believe we understand the best places to procure our various product categories. We currently source our products from more than 240 vendors worldwide and have developed long-term relationships with many of them. We often collaborate with our vendors to design and manufacture products for us to address emerging customer preferences that we observe in our stores and markets. We procure the majority of our products directly from the manufacturers, which eliminates additional costs from exporters, importers, wholesalers and distributors. We believe direct sourcing is a key competitive advantage, as many of our specialty retail flooring competitors are too small to have the scale or the resources to work directly with suppliers. Over the past several years, we have established a Global Sourcing and Compliance Department to, among other things, enhance our policies and procedures with respect to addressing compliance with appropriate regulatory bodies, including compliance with the requirements of the Lacey Act of 1900 (as amended, the "Lacey Act"), the California Air Resources Board ("CARB") and the Environmental Protection Agency ("EPA"). We also utilize third-party consultants for audits, testing and surveillance to ensure product safety and compliance. Additionally, we have invested in technology and personnel to collaborate throughout the entire supply chain process to support our direct sourcing model, which has improved our ability to find, manage and source trend-right merchandise quickly and at lower costs, allowing us to offer products at low prices while maintaining attractive gross margins.

*Highly Experienced Management Team with a Proven Track Record.* Led by our Chief Executive Officer, Tom Taylor, our management team brings substantial expertise from leading retailers and other companies across various core functions, including store operations, merchandising, marketing, real estate, e-commerce, supply chain management, finance, legal and information technology. Tom Taylor, who joined us in 2012, spent 23 years at The Home Depot, where he most recently served as Executive Vice President of Merchandising and Marketing with responsibility for all stores in the United States and Mexico. Over the course of his career at The Home Depot, Tom Taylor helped expand the store base from fewer than 15 stores to over 2,000 stores. Our Executive Vice President and Chief Merchandising Officer, Lisa Laube, has over 30 years of merchandising and leadership experience with leading specialty retailers, including most recently as President of Party City. Our Executive Vice President and Chief Financial Officer, Trevor Lang, brings more than 20 years of accounting and finance experience, including 18 years of Chief Financial Officer and Vice President of Finance experience at public companies, including most recently as the Chief Financial Officer and Chief Administrative Officer of Zumiez Inc. Our entire management team drives our organization with a focus on strong merchandising, superior customer experience, expanding our store footprint, and fostering a strong, decentralized culture. We believe our management team is an integral component of our achieving strong financial results.

## **Our Growth Strategy**

We expect to continue to drive our strong net sales and profit growth through the following strategies:

*Open Stores in New and Existing Markets.* We believe there is an opportunity to significantly expand our store base in the United States from 100 warehouse-format stores currently to approximately 400 stores nationwide over the next 10-15 years based on our internal research with respect to housing density, demographic data, competitor concentration and other variables in both new and existing markets. We plan to target new store openings in both new and existing, adjacent and underserved markets. We have a disciplined approach to new store development, based on an analytical, research-driven site selection method and a rigorous real estate



approval process. We believe our new store model delivers strong financial results and returns on investment, targeting net sales on average of \$10 million to \$13 million and positive four-wall adjusted EBITDA in the first year, pre-tax payback in approximately two years and cash-on-cash returns of greater than 50% in the third year. On average, our stores opened after 2011 have exceeded this model. Over the past several years, we have made significant investments in personnel, information technology, warehouse infrastructure and connected customer strategies to support our current growth and the expansion of our stores. We intend to grow our store base by approximately 20% annually for the next several years. The performance of our new stores opened over the last three years, the performance of our older stores over that same time frame, our disciplined real estate strategy and the track record of our management team in successfully opening retail stores support our belief in the significant store expansion opportunity.

*Increase Comparable Store Sales.* We expect to grow our comparable store sales by continuing to offer our customers a dynamic and expanding selection of compelling, value-priced hard surface flooring and accessories while maintaining strong service standards for our customers. We regularly introduce new products into our assortment through our category product line review process, including collaboration with our vendors to bring to market innovative products such as water-resistant laminates. Because almost half of our stores have been opened for less than three years, we believe they will continue to drive comparable store sales growth as they ramp to maturity. We believe that we can continue to enhance our customer experience by focusing on service, optimizing sales and marketing strategies, investing in store staff and infrastructure, remodeling existing stores and improving visual merchandising and the overall aesthetic appeal of our stores. We also believe that growing our proprietary credit offering, further integrating connected customer strategies and enhancing other key information technology, will contribute to increased comparable store sales. As we increase awareness of Floor & Decor's brand, we believe there is a significant opportunity to gain additional market share, especially from independent flooring retailers and large format home improvement retailers. We are also adding adjacent categories that align with flooring projects like frameless glass in the bathroom and customized countertops for the kitchen. We believe the combination of these initiatives plus the expected growth of the hard surface flooring category described in more detail under "Our Industry" below will continue to drive strong comparable store sales growth.

*Continue to Invest in the Pro Customer.* We believe our differentiated focus on Pro customers has created a competitive advantage for us and will continue to drive our net sales growth. We will invest in gaining and retaining Pro customers due to their frequent and high-ticket purchases, loyalty and propensity to refer other potential customers. We have made important investments in the Pro services regional team to better recruit and train the Pro services team in each store, new technology such as integrated CRM software to help us further penetrate and grow our Pro business, dedicated phone lines for our Pro customers to call and text, commercial credit and open account terms, jobsite delivery, a dedicated website for Pro customers, training on technical flooring installation solutions, and tools to facilitate large commercial jobs sourced throughout the store. We plan to further invest in initiatives to increase speed of service, improve financing solutions, leverage technology, elevate our Pro branding, dedicate additional store staffing to support Pro customers and enhance the in-store experience for our Pro customers. We have implemented a "Pro Zone" in a majority of our stores that focuses on the specific needs of the Pro customer. After successful tests, we completed the roll out of our Pro loyalty program to all stores in the second half of fiscal 2018. Additionally, we communicate our value proposition and various Pro-focused offerings by hosting a number of Pro networking events. Building on our success in serving the Pro customer, in 2016 we entered the adjacent commercial sales channel, thereby increasing the size of the addressable market we serve. Our commercial effort, which we have branded F&D Commercial, initially targets corporate customers with large flooring needs across the hospitality, multi-family and retail sectors. We believe Pro customers will continue to be an integral part of our sales growth, and the commercial channel will provide incremental revenue and profit opportunities in the future.

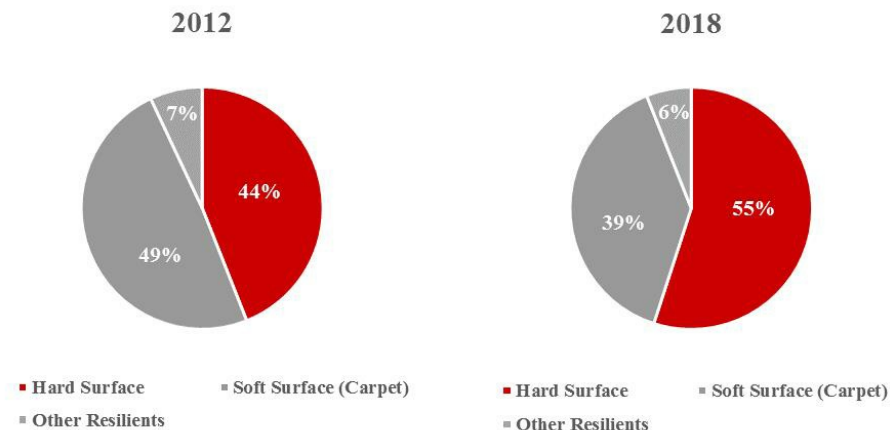
*Expand Our "Connected Customer" Experience.* Floor & Decor's online experience allows our Pro, BIY and DIY customers to explore our product selection and design ideas before and after visiting our stores and offers the convenience of making online purchases for delivery or pick up in-store. We believe our online platform reflects our brand attributes and provides a powerful tool to educate, inspire and engage our consumers, and we view our website and multi-channel strategies as leading our brand. Our research indicates that 72% of our shoppers have visited our website. We continuously invest in our connected customer strategies to improve how our customers experience our brand. For example, we regularly update our website, which provides our customers with inspirational vignettes, videos, products and education. Additional initiatives include: (i) implementing our new CRM to obtain a single view of our customers, (ii) developing personalized content based on location, purchase and browsing history, (iii) developing more relevant content and improved search and purchasing tools to help customers add decorative and installation accessories, (iv) creating frequently asked questions to help customers choose the best product for their jobs and (v) implementing online scheduling tools to help customers access our designers. We believe this reinforces our unique customer value proposition and ultimately drives sales. Currently, e-commerce sales represent approximately 8% of our total net sales. While the hard surface flooring category has a relatively low penetration of e-commerce sales due to the nature of the product, we believe our connected customer presence represents an attractive growth opportunity to drive consumers to Floor & Decor.

*Enhance Margins Through Increased Operating Leverage.* Since 2011, we have invested significantly in our sourcing and distribution network, integrated IT systems and corporate overhead to support our growth. We expect to leverage these investments as we grow our net sales. Additionally, we believe operating margin improvement opportunities will include enhanced product sourcing processes and overall leveraging of our store-level fixed costs, existing infrastructure, supply chain, corporate overhead and other fixed costs resulting from increased sales productivity. We anticipate that the planned expansion of our store base and growth in comparable store sales will also support increasing economies of scale.

**Our Industry**

Floor & Decor operates in the large, growing and highly fragmented \$13 billion hard surface flooring market (in manufacturers’ dollars), which is part of the larger \$22 billion U.S. floor coverings market (in manufacturers’ dollars) based on internal research as well as a 2018 research report by Catalina Research, Inc., a leading provider of market research for the floor coverings industry (the “Catalina Floor Coverings Report”). We estimate that, after retail markup, the addressable hard surface flooring market for Floor & Decor is \$21 billion, of which we represent approximately 8%. The competitive landscape of the hard surface flooring market includes big-box home improvement centers, national and regional specialty flooring retailers, and independent flooring retailers. We believe we benefit from growth in the overall hard surface flooring market, which grew on average 8% per year from 2012 to 2018 and is estimated to grow on average 3%-6% per year from 2019 through 2023, assuming no negative economic cycle, housing downturn or recession. We believe that growth in the hard surface flooring market has been and will continue to be driven by home remodeling demand drivers such as the aging household inventory, millennials forming households, existing home sales, rising home equity values and the secular shift from carpet to hard surface flooring. In addition, we believe we have an opportunity to increase our market share as our competitors are unable to compete with our combination of price, service and in-stock assortment.

Based on our internal market research, key long-term industry trends include increasing spend on home renovations, aging of the existing housing stock, rising level of home ownership, growing average size of homes and favorable demographic trends. Throughout this decade, hard surface flooring has consistently taken share from carpet as a percentage of the total floor coverings market, increasing from 44% of the market in 2012 to 55% in 2018. Historically, mix shift towards hard surface flooring has been driven by product innovation, changing consumer preferences, better hygiene qualities, increasing ease of installation and higher durability. Product innovation, which has been aided by the increasing use of technology such as inkjet tile printing, waterproof wood-look flooring and water-resistant laminates, and non-traditional uses of hard surface flooring including walls, fireplaces and patios, has increased the size of the hard surface flooring market and has allowed us to better serve customer needs.



We believe we have an opportunity to continue to gain share in the hard surface flooring market with the largest selection of tile, wood, laminate, vinyl, natural stone, decorative accessories and installation accessories. Our strong focus on the customer

experience drives us to remain innovative and locally relevant while maintaining low prices and in-stock merchandise in a one-stop shopping destination.

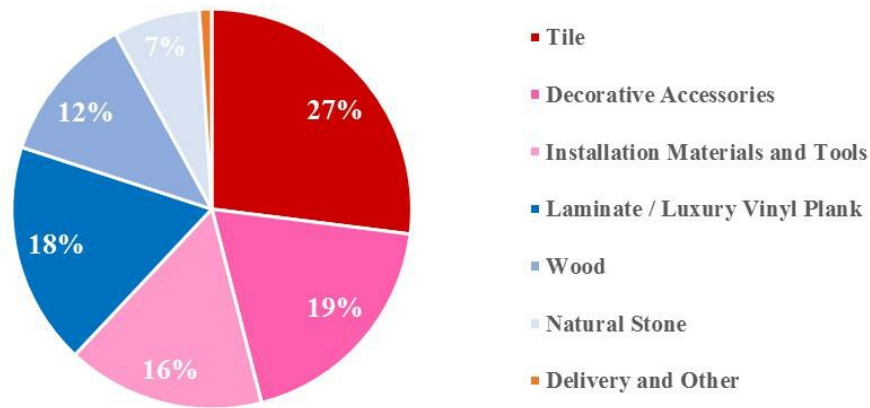
### **Our Products**

We offer an assortment of tile, wood, laminate, vinyl, and natural stone flooring, along with decorative and installation materials at everyday low prices. Our objective is to carry a broad and deep in-stock product offering in order to be the one-stop destination for our customer's entire project needs. We seek to showcase products in our stores and online to provide multiple avenues for inspiration throughout a customer's decision-making process.

Our strategy is to fulfill the product needs of our Pro, DIY and BIY customers with our extensive assortment, in-stock inventory and merchandise selection across a broad range of price points. We offer bestseller products in addition to the more unique, hard to find items that we believe our customers have come to expect from us. We source our products from around the world, constantly seeking new and exciting merchandise to offer our customers. Our goal is to be at the forefront of hard surface flooring trends in the market, while offering low prices given our ability to source directly from manufacturers and quarries.

We utilize a regional merchandising strategy in order to carry products in our stores that cater to the preferences of our local customer base. This strategy is executed by our experienced merchandising team, which consists of category merchants and regional merchants, who work with our individual stores to ensure they have the appropriate product mix for their location. Our category merchants are constantly seeking new products and following trends by attending trade shows and conferences, as well as by meeting with vendors around the world. We schedule regular meetings to review information gathered and make future product decisions. This constant connectivity between our stores, regional merchants, category merchants, and our vendors allows us to quickly bring new, innovative, and compelling products to market.

Our fiscal 2018 net sales by key product categories are set forth below:



Category	Products Offered	Select Product Highlights
Tile	Porcelain, White Body, Ceramic	We offer a wide selection of Porcelain and Ceramic tiles from 4"x4" all the way up to 24"x72" and 48"x48". We source many products directly from Italy, where many design trends in tile originate. We offer traditional stone looks as well as wood-looking planks and contemporary products like cement-look and vein cut styles. We work with many factories in the United States, China, Italy, Mexico, Brazil, Turkey and other countries to bring the most in-demand styles at low prices.
Wood	Solid Prefinished Hardwood, Solid Unfinished Hardwood, Engineered Hardwood, Bamboo, Cork, Wood Wall	We sell common species such as Oak, Walnut, Birch, Hickory and Maple but also exotics such as Bamboo, Brazilian Cherry, and Acacia, all in multiple colors. Our wood flooring comes in multiple widths from 2 1/4" up to 9 3/4" wide planks. Customers have the option of buying prefinished or unfinished flooring in many of our stores.
Natural Stone	Marble, Travertine, Limestone, Slate, Granite	Natural stone is quarried around the world, and we typically buy directly from the source. For example, we buy natural stones from Italy, Spain, Turkey, Portugal, India, and China. We work with factories in these countries and others to cut stone tiles in many sizes, finishes and colors.

<b>Category</b>	<b>Products Offered</b>	<b>Select Product Highlights</b>
Laminate/Luxury Vinyl Plank	Laminate Flooring, Luxury Vinyl, Engineered/Composite Vinyl	Laminate, AquaGuard® water-resistant laminate, NuCore®, DuraLux® Rigid and Luxury Vinyl plank flooring is offered in styles that mimic our bestselling tile and wood species, colors and finishes. Our product offers a full range of installation methods, many are water-resistant to waterproof, and all are great for customers who want the beauty of real hardwood and stone but the ease of maintenance and durability that laminate and luxury vinyl offer.
Decorative Accessories	Glass, Natural Stone, Tile Mosaics and Decorative Tiles, Decorative Trims, Prefabricated Countertops, Medallions, Wall Tile	With over 800 choices in glass, stone mosaics and decoratives, we can customize nearly any look or style a customer desires. This trend-forward and distinctive category is a favorite of our designers and offers customers an inexpensive way to quickly update a backsplash or shower.
Installation Materials and Tools	Grout, Underlayment, Adhesives, Mortar, Backer Board, Power and Hand Tools, Wood Moldings, Wood Glues, Blades	This category offers everything a customer needs to complete his or her project, including backer board, mortar, grout, underlayment, adhesives, wood glues, molding and tools. We sell top brands, which we believe are highly valued by our customers.

**Stores**

We operate 100 warehouse-format stores across 28 states and one small 5,500 square foot design center. Most of our stores are situated in highly visible retail and industrial locations. Our warehouse-format stores average approximately 75,000 square feet and carry on average approximately 3,800 flooring, decorative and installation accessory SKUs, which equates to approximately 1.3 million square feet of flooring products or \$2.5 million of inventory at cost.

Each of our stores is led by a store manager who holds the title Chief Executive Merchant and is supported by an operations manager, department managers, a design team, and a Pro sales team. Our store managers focus on providing superior customer service and creating customized store offerings that are tailored to meet the specific needs of their stores. Beyond the store managers, each store is staffed with associates, the number of whom vary depending on sales volume and size of the store. We dedicate significant resources to training all of our new store managers through Floor & Decor University and in the field across all product areas, with store-level associates receiving certification on specific product areas. Ongoing training and continuing education are provided for all employees throughout the year.

We believe there is an opportunity to significantly expand our store base in the United States from our 100 warehouse-format stores currently to approximately 400 stores nationwide within the next 10-15 years based on our internal research with respect to housing density, demographic data, competitor concentration and other variables in both new and existing markets. For the next several years, we plan to grow our store base by approximately 20% per year, with approximately half being opened in existing geographies and approximately half being opened in new markets. We have developed a disciplined approach to new store development, based on an analytical, research-driven method to site selection and a rigorous real estate review and approval process. By focusing on key demographic characteristics for new site selection, such as aging of homes, length of home ownership and median income, we expect to open new stores with attractive returns.

When opening new stores, inventory orders are placed several months prior to a new store opening. Significant investment is made in building out or constructing the site, hiring and training employees in advance, and advertising and marketing the new store through pre-opening events to draw the flooring industry community together. Each new store is thoughtfully designed with store

interiors that include interchangeable displays on wheels, racking to access products and stand-up visual displays to allow ease of shopping and an exterior highlighted by a large, bold Floor & Decor sign. The majority of our stores have design centers that showcase project ideas to further inspire our customers, and, in all of our stores, we employ experienced designers to provide design consulting to our customers free of charge. Additionally, we have rolled out “Pro Zones”, which are dedicated areas offering a variety of services to Pro customers, in a majority of our stores.

Our new store model targets a store size of 60,000-80,000 square feet, total initial net cash investment of approximately \$4 million to \$5 million, targeting net sales on average of \$10 million to \$13 million and positive four-wall Adjusted EBITDA in the first year, pre-tax payback in two to three years and cash-on-cash returns of greater than 50% in the third year. On average, our stores opened after 2011 have exceeded this model. We believe the success of our stores across geographies and vintages supports the portability of Floor & Decor into a wide range of markets. The performance of our new stores is inherently uncertain and is subject to numerous factors that are outside of our control. As a result, we cannot assure you that our new stores will achieve our target results.

### **Connected Customer**

Our website and our call center are important parts of our integrated connected customer strategy. We aim to elevate the customer experience through our website *FloorandDecor.com*. Growing our e-commerce sales provides us with additional opportunity to enhance our connected customer experience for our customers. Home renovation and remodeling projects typically require significant investments of time and money from our DIY customers, and they consequently plan their projects carefully and conduct extensive research online. *FloorandDecor.com* is an important tool for engaging our DIY customers throughout this process, educating them on our product offerings and providing them with design ideas. Our Pro customers use the website to browse our broad product assortment, to continually educate themselves on new techniques and trends and to share our virtual catalogue and design ideas with their customers. In addition, sales associates at our call center are available to assist our customers with their projects and questions. We designed the website to be a reflection of our stores and to promote our wide selection of high quality products and low prices. To this end, we believe the website provides not only the same region-specific product selection that customers can expect in our stores, but also the opportunity to extend our assortment by offering our entire portfolio of products.

In addition to highlighting our broad product selection, we believe *FloorandDecor.com* offers a convenient opportunity for customers to purchase products online and pick them up in our stores. Approximately 77% of our e-commerce sales are picked up in-store. As we continue to grow, we believe connected customer will become an increasingly important part of our strategy.

### **Marketing and Advertising**

We use a multi-platform approach to increasing Floor & Decor’s brand awareness, while historically maintaining a low average advertising to net sales ratio of approximately 3%. We use traditional advertising media, combined with social media and online marketing, to share the Floor & Decor story with a growing audience. We take the same customized approach with our marketing as we do with our product selection; each region has a varied media mix based on local trends and what we believe will most efficiently drive sales. To further enhance our targeting efforts, our store managers have significant input into their respective stores’ marketing spend.

A key objective of our messaging is to make people aware of our stores, products and services. Based on our internal research, we estimate the conversion rate from a customer visiting one of our stores to purchasing our products is 76%.

As part of our focus on local markets, our stores have events that promote Floor & Decor as a hub for the local home improvement community. We feature networking events for Pro customers, giving them a chance to meet our sales teams, interact with others in the home improvement industry and learn about our newest products. For DIY customers, we regularly offer how-to classes on product installation. We believe these events serve to raise the profile of the Floor & Decor stores in our communities while showcasing our tremendous selection of products and services.

We want our customers to have a great experience at their local Floor & Decor store. Through our TV and radio commercials, print and outdoor ads, in-store flyers, online messaging and community events, we show our customers that we are a trusted resource with a vast selection, all at a low price.

## **Sourcing**

Floor & Decor has a well-developed and geographically diverse supplier base. We source our industry leading merchandise assortment from over 240 suppliers in over 21 countries, and maintain good relationships with our vendors. No supplier accounts for more than 10% of our net sales, other than one supplier that accounts for approximately 13% of our net sales. We are focused on bypassing agents, brokers, distributors and other middlemen in our supply chain in order to reduce costs and lead time. Over the past several years, we have established a Global Sourcing and Compliance Department to, among other things, develop and implement policies and procedures in order to address compliance with appropriate regulatory bodies, including compliance with the requirements of the Lacey Act, CARB and the EPA. In addition, we utilize third-party consultants for audits, testing and surveillance to ensure product safety and compliance. Additionally, we have invested in technology and personnel to collaborate throughout the entire supply chain process. We believe that our direct sourcing model and the resulting relationships we have developed with our suppliers are distinct competitive advantages. The cost savings we achieve by directly sourcing our merchandise enable us to offer our customers low prices. Additionally, our close relationships with suppliers allow us to collaborate with them directly to develop and quickly introduce innovative and quality products that meet our customers' evolving tastes and preferences at low prices. We plan to continue increasing the percentage of merchandise that we directly source from suppliers.

## **Distribution and Order Fulfillment**

Merchandise inventory is our most significant working capital asset and is considered "in-transit" or "available for sale", based on whether we have physically received the products at an individual store location or in one of our three distribution centers. In-transit inventory generally varies due to contractual terms, country of origin, transit times, international holidays, weather patterns and other factors, but approximately 16% of our inventory is in-transit, while roughly 84% is available for sale in our stores or at one of our three distribution centers.

We have invested significant resources to develop and enhance our distribution network. We have three distribution centers strategically located across the United States in port cities near Savannah, Georgia; Houston, Texas; and Los Angeles, California. We closed our distribution center near Miami, Florida in the first quarter of fiscal 2018. Third-party brokers arrange the shipping of our international and domestic purchases to our distribution centers and stores and bill us for shipping costs according to the terms of the purchase agreements with our suppliers. We are typically able to transport inventory from our distribution centers to our stores in less than one week. This quick turnaround time enhances our ability to maintain project-ready quantities of the products stocked in our stores. To further strengthen our distribution capabilities, we have converted all of our distribution centers to Company-operated facilities. In conjunction with the change in responsibility, we have implemented a warehouse management and transportation management system tailored to our unique needs across all three distribution centers. We believe this system will increase service levels, reduce shrinkage and damage, help us better manage our inventory and allow us to better implement our connected customer initiatives.

In the fourth quarter of fiscal 2017, we began operating in a newly constructed, leased 1.4 million square foot distribution center near Savannah, Georgia. In December 2017, we relocated all of the existing inventory from our prior leased 378,000 square foot distribution center located near Savannah, Georgia to this new distribution center, and in the first quarter of fiscal 2018, we relocated all of the existing inventory from our 322,000 square foot leased distribution center near Miami, Florida to this new distribution center. We exited our lease on the 378,000 square foot distribution center near Savannah, Georgia in the first quarter of fiscal 2018 and plan to exit our lease on the 322,000 square foot distribution center near Miami, Florida in 2021.

We anticipate opening a new distribution center in Maryland in late fiscal 2019, and we plan to continue to seek further opportunities to enhance our distribution capabilities and align them with our strategic growth initiatives.

## **Management Information Systems**

We believe that technology plays a crucial role in the continued growth and success of our business. We have sought to integrate technology into all facets of our business, including supply chain, merchandising, store operations, point-of-sale, e-commerce, finance, accounting and human resources. The integration of technology allows us to analyze the business in real time and react accordingly. Our sophisticated inventory management system is our primary tool for forecasting, placing orders and managing in-stock inventory. The data-driven platform includes sophisticated forecasting tools based on historical trends in sales, inventory levels and vendor lead times at the store and distribution center level by SKU, allowing us to support store managers in their regional merchandising efforts. We rely on the forecasting accuracy of our system to maintain the in-stock, project-ready quantities that our customers rely on. In addition, our employee training certifications are entirely electronic, allowing us to effectively track the

competencies of our staff and manage talent across stores. We believe that our systems are sufficiently scalable to support the continued growth of the business.

### **Competition**

The retail hard surface flooring market is highly fragmented and competitive. We face significant competition from large home improvement centers, national and regional specialty flooring chains and independent flooring retailers. Some of our competitors are organizations that are larger, are better capitalized, have existed longer, have product offerings that extend beyond hard surface flooring and related accessories, and have a more established market presence with substantially greater financial, marketing, personnel and other resources than we have. In addition, while the hard surface flooring category has a relatively low threat of new internet-only entrants due to the nature of the product, the growth opportunities presented by e-commerce could outweigh these challenges and result in increased competition in this portion of our connected customer strategy. Further, because the barriers to entry into the hard surface flooring industry are relatively low, manufacturers and suppliers of flooring and related products, including those whose products we currently sell, could enter the market and start directly competing with us.

We believe that the key competitive factors in the retail hard surface flooring industry include:

- product assortment;
- product innovation;
- in-store availability of products in project-ready quantities;
- product sourcing;
- product presentation;
- customer service;
- store management;
- store location; and
- low prices.

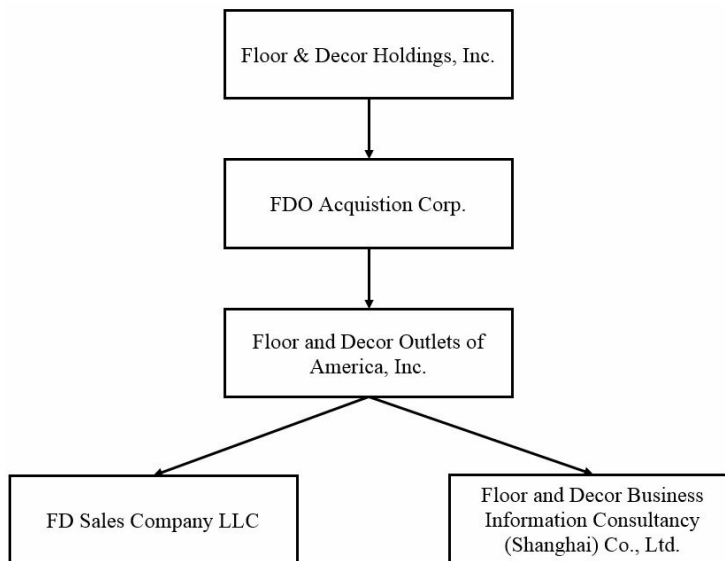
We believe that we compete favorably with respect to each of these factors by providing a highly diverse selection of products to our customers, at an attractive value, in appealing and convenient retail stores.

### **Our Structure**

Floor & Decor Holdings, Inc. (formerly known as FDO Holdings, Inc.) was incorporated as a Delaware corporation in October 2010 in connection with our Sponsors' (as defined below) acquisition of Floor & Decor Outlets of America, Inc. ("F&D") in November 2010, which in turn converted from a Georgia corporation into a Delaware corporation in connection therewith.



The following chart illustrates our current corporate structure:



← Indicates 100% Ownership

**Employees**

As of December 27, 2018, we had 6,566 employees, 4,707 of whom were full-time and none of whom were represented by a union. Of these employees, 5,742 work in our stores, 579 work in corporate, store support, infrastructure, e-commerce or similar functions, 232 work in distribution centers, and 13 work in our Asia sourcing office in Shanghai, China. We believe that we have good relations with our employees.

**Government Regulation**

We are subject to extensive and varied federal, state and local laws and regulations, including those relating to employment, the environment, protection of natural resources, import and export, advertising, labeling, public health and safety, product safety, zoning and fire codes. We operate our business in accordance with standards and procedures designed to comply with applicable laws and regulations. Compliance with these laws and regulations has not historically had a material effect on our financial condition or operating results; however, the effect of compliance in the future cannot be predicted.

Our operations and properties are also subject to federal, state and local laws and regulations governing the environment, environmental protection of natural resources and health and safety, including 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. Except to the extent of the capital expenditures related to our initiatives described below, compliance with these laws and regulations has not historically had a material effect on our financial condition or operating results, but we cannot predict the effect of compliance in the future.

In particular, certain of our products are subject to laws and regulations relating to the importation, exportation, acquisition or sale of certain plants and plant products, including those illegally harvested (which is prohibited by the Lacey Act), and the emissions of hazardous materials (which in California is governed by regulations promulgated by CARB and federally by regulations promulgated by the EPA). We have established a Global Sourcing and Compliance Department to, among other things, address these requirements, and we work with third-party consultants to assist us in designing and implementing compliance programs relating to the requirements of the Lacey Act, CARB and the EPA. Further, we could incur material compliance costs or be subject to compliance

liabilities or claims in the future, especially in the event new laws or regulations are adopted or there are 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 also support social and environmental responsibility among our supplier community and endeavor to enter into vendor agreements with our suppliers that contain representations and warranties concerning environmental, labor and health and safety matters.

#### **Insurance and Risk Management**

We use a combination of insurance and self-insurance to provide for potential liability for workers' compensation, general liability, product liability, director and officers' liability, team member healthcare benefits, and other casualty and property risks. Changes in legal trends and interpretations, variability in inflation rates, changes in workers' compensation and general liability premiums and deductibles, changes in the nature and method of claims settlement, benefit level changes due to changes in applicable laws, insolvency of insurance carriers, and changes in discount rates could all affect ultimate settlements of claims. We evaluate our insurance requirements on an ongoing basis to ensure we maintain adequate levels of coverage.

#### **Legal Proceedings**

We are engaged in various legal actions, claims and proceedings arising in the ordinary course of business, including claims related to breach of contracts, products liabilities, intellectual property matters and employment related matters resulting from our business activities. As with most actions such as these, an estimation of any possible and/or ultimate liability cannot always be determined. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

#### **Trademarks and other Intellectual Property**

As of February 20, 2019, we have 76 registered marks and several pending trademark applications in the United States. We regard our intellectual property, including our over 50 proprietary brands, as having significant value, and our brand is an important factor in the marketing of our products. Accordingly, we have taken, and continue to take, appropriate steps to protect our intellectual property.

#### **Available Information**

We maintain a website at [www.FloorandDecor.com](http://www.FloorandDecor.com). The information on or available through our website is not, and should not be considered, a part of this Annual 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 (the "SEC") free of charge on our website as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC.

**ITEM 1A. RISK FACTORS .**

*You should carefully consider the risks described below, together with all of the other information included in this Annual Report, including our consolidated financial statements and the related notes thereto, before making an investment decision. The risks and uncertainties set out below are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition and operating results. If any of the following events occur, our business, financial condition and operating results could be materially and adversely affected. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment.*

**Risks Related to our Business**

***Our business, financial condition and operating results are dependent on general economic conditions and discretionary spending by our customers, which in turn are affected by a variety of factors beyond our control. If such conditions deteriorate, our business, financial condition and operating results may be adversely affected.***

Our business, financial condition and operating results are affected by general economic conditions and discretionary spending by our customers. Such general economic conditions and discretionary spending are beyond our control and are affected by, among other things:

- consumer confidence in the economy;
- unemployment trends;
- consumer debt levels;
- consumer credit availability;
- data security and privacy concerns;
- the housing market, including housing turnover and whether home values are rising or declining;
- energy prices;
- interest rates and inflation;
- price deflation, including due to low-cost imports;
- slower rates of growth in real disposable personal income;
- natural disasters and unpredictable weather;
- national security concerns and other geopolitical risks;
- uncertain U.S. political conditions, including the possibility of future government shutdowns;
- trade relations and tariffs;
- tax rates and tax policy; and
- other matters that influence consumer confidence and spending.

If such conditions deteriorate, our business, financial condition and operating results may be adversely affected. In addition, increasing volatility in financial and capital markets may cause some of the above factors to change with a greater degree of frequency and magnitude than in the past.

***The hard surface flooring industry depends on home remodeling activity and other important factors.***

The hard surface flooring industry is highly dependent on the remodeling of existing homes, businesses and, to a lesser extent, new home construction. In turn, remodeling and new home construction depend on a number of factors that are beyond our control, including interest rates, tax policy, trade policy, employment levels, consumer confidence, credit availability, real estate prices, existing home sales, demographic trends, weather conditions, natural disasters and general economic conditions. In particular:

- the national economy or any regional or local economy where we operate could weaken;
- home-price appreciation could slow or turn negative;
- regions where we have stores that could be impacted by hurricane, fire, or other natural disasters (including those due to the effects of climate change such as increased storm severity, drought, wildfires, and potential flooding due to rising sea levels and storm surges);
- interest rates could rise;
- credit could become less available;
- tax rates and/or health care costs could increase; or
- fuel costs or utility expenses could increase.

Any one or a combination of these factors could result in decreased demand for our products, reduce spending on homebuilding or remodeling of existing homes or cause purchases of new and existing homes to decline. While the vast majority of our net sales are derived from home remodeling activity as opposed to new home construction, a decrease in any of these areas would adversely affect our business, financial condition and operating results.

***Any failure by us to successfully anticipate trends may lead to loss of consumer acceptance of our products, resulting in reduced net sales.***

Each of our stores is stocked with a customized product mix based on consumer demands in a particular market. Our success therefore depends on our ability to anticipate and respond to changing trends and consumer demands in these markets in a timely manner. If we fail to identify and respond to emerging trends, consumer acceptance of our merchandise and our image with current or potential customers may be harmed, which could reduce our net sales. Additionally, if we misjudge market trends, we may significantly overstock unpopular products, incur excess inventory costs and be forced to reduce the sales price of such products or incur inventory write-downs, which would adversely affect our operating results. Conversely, shortages of products that prove popular could also reduce our net sales through missed sales and a loss of customer loyalty.

***If we fail to successfully manage the challenges that our planned new store growth poses or encounter unexpected difficulties during our expansion, our operating results and future growth opportunities could be adversely affected.***

We have 100 warehouse-format stores and one small-format standalone design center located throughout the United States as of December 27, 2018. We plan to open 20 warehouse-format stores during fiscal 2019 and to increase the number of new stores that we open during each of the next several years thereafter. We also plan to relocate a warehouse-format store in fiscal 2019. This growth strategy and the investment associated with the development of each new store may cause our operating results to fluctuate and be unpredictable or decrease our profits. We cannot ensure that store locations will be available to us, or that they will be available on terms acceptable to us. If additional retail store locations are unavailable on acceptable terms, we may not be able to carry out a significant part of our growth strategy or our new stores' profitability may be lower. Our future operating results and ability to grow will depend on various other factors, including our ability to:

- successfully select new markets and store locations;
- negotiate leases on acceptable terms;

- attract, train and retain highly qualified managers and staff;
- maintain our reputation of providing quality, safe and compliant products; and
- manage store opening costs.

In addition, consumers in new markets may be less familiar with our brand, and we may need to increase brand awareness in such markets through additional investments in advertising or high cost locations with more prominent visibility. Stores opened in new markets may have higher construction, occupancy or operating costs, or may have lower net sales, than stores opened in the past. In addition, laws or regulations in these new markets may make opening new stores more difficult or cause unexpected delays. Newly opened stores may not succeed or may reach profitability more slowly than we expect, and the ramp-up to profitability may become longer in the future as we enter more markets and add stores to markets where we already have a presence. Future markets and stores may not be successful and, even if they are successful, our comparable store sales may not increase at historical rates. To the extent that we are not able to overcome these various challenges, our operating results and future growth opportunities could be adversely affected.

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

We operate in the hard surface flooring industry, which is highly fragmented and competitive. We face competition from large home improvement centers, national and regional specialty flooring chains, Internet-based companies and independent flooring retailers. Among other things, we compete on the basis of breadth of product assortment, low prices, and the in-store availability of the products we offer in project-ready quantities, as well as the quality of our products and customer service. As we expand into new and unfamiliar markets, we may experience different competitive conditions than in the past.

Some of our competitors are organizations that are larger, are better capitalized, have existed longer, have product offerings that extend beyond hard surface flooring and related accessories and have a more established market presence with substantially greater financial, marketing, personnel and other resources than we have. In addition, while the hard surface flooring category has a relatively low threat of new internet-only entrants due to the nature of the product, the growth opportunities presented by e-commerce could outweigh these challenges and result in increased competition. Competitors may forecast market developments more accurately than we do, offer similar products at a lower cost or adapt more quickly to new trends and technologies or evolving customer requirements than we do. Further, because the barriers to entry into the hard surface flooring industry are relatively low, manufacturers and suppliers of flooring and related products, including those whose products we currently sell, could enter the market and start directly competing with us. Intense competitive pressures from any of our present or future competitors could cause price declines, decrease demand for our products and decrease our market share. Also, if we continue to grow and become more well-known, other companies may change their strategies to present new competitive challenges. Moreover, in the future, changes in consumer preferences may cause hard surface flooring to become less popular than other types of floor coverings. Such a change in consumer preferences could lead to decreased demand for our products.

All of these factors may harm us and adversely affect our net sales, market share and operating results.

***U.S. policies related to global trade and tariffs could adversely affect our business, financial condition and results of operations.***

The current domestic and international political environment, including existing and potential changes to U.S. policies related to global trade and tariffs, have resulted in uncertainty surrounding the future state of the global economy. In September 2018, the U.S. imposed tariffs of 10% on many products from China, and the U.S. administration has announced an intention to increase that amount to 25% in March 2019 if a trade agreement cannot be reached. We import approximately 50% of the products we sell from China, the vast majority of which are impacted by these tariffs. Any further expansion in the types or levels of tariffs implemented has the potential to negatively impact our business, financial condition and results of operations. Additionally, there is a risk that the U.S. tariffs on imports are met with tariffs on U.S. produced exports and that a broader trade conflict could ensue, which has the potential to significantly impact global trade and economic conditions. Potential costs and any attendant impact on pricing arising from these tariffs and any further expansion in the types or levels of tariffs implemented could require us to modify our current business practices and could adversely affect our business, financial condition and results of operations.

***Any disruption in our distribution capabilities or our related planning and control processes may adversely affect our business, financial condition and operating results.***

Our success is highly dependent on our planning and distribution infrastructure, which includes the ordering, transportation and distribution of products to our stores and the ability of suppliers to meet distribution requirements. We also need to ensure that we continue to identify and improve our processes and supply chain and that our distribution infrastructure and supply chain keep pace with our anticipated growth and increased number of stores. The cost of these enhanced processes could be significant and any failure to maintain, grow, or improve them could adversely affect our business, financial condition and operating results. Due to our rapid expansion, we have had to significantly increase the size of our distribution centers. Based on our growth intentions we plan to add additional distribution centers or increase the size of our existing distribution centers in the future. Increasing the size of our distribution centers may decrease the efficiency of our distribution costs.

We manage our three distribution centers internally rather than rely on independent third-party logistics providers. If we are not able to manage our distribution centers successfully or at a lower cost than with third-party logistics providers, it could adversely affect our business, financial condition and operating results. We expect to open a new distribution center in Maryland in late fiscal 2019. As we work towards the consummation of this transition, we may incur unexpected costs, and our ability to distribute our products may be adversely affected. Any disruption in the transition to or operation of our distribution centers could have an adverse impact on our business, financial condition and operating results. In addition, our long-term plan contemplates the ability to sublet a portion of our previously occupied distribution centers. Any failure to do so on favorable terms could have a negative impact on our financial condition and operating results.

Our success is also dependent on our ability to provide timely delivery to our customers. Our business could also be adversely affected if fuel prices increase or there are delays in product shipments due to freight difficulties, inclement weather, strikes by our employees or employees of third-parties involved in our supply chain, or other difficulties. If we are unable to deliver products to our customers on a timely basis, they may decide to purchase products from our competitors instead of from us, which would adversely affect our business, financial condition and operating results.

***Our operating results may be adversely affected by fluctuations in material and energy costs beyond our control.***

Our operating results may be affected by the wholesale prices of hard surface flooring products, setting and installation materials and the related accessories that we sell. These prices may fluctuate based on a number of factors beyond our control, including the price of raw materials used in the manufacture of hard surface flooring, energy costs, changes in supply and demand, concerns about inflation, general economic conditions, labor costs, competition, import duties, tariffs, currency exchange rates, government regulation, the impact of natural disasters (including those due to the effects of climate change), duty and other import costs. In particular, energy costs have fluctuated dramatically in the past and may fluctuate in the future. These fluctuations may result in an increase in our transportation costs for distribution from the manufacturer to our distribution centers and from our distribution centers to our retail stores, utility costs for our distribution centers and retail stores and overall costs to purchase products from our suppliers.

We may not be able to adjust the prices of our products, especially in the short-term, to recover these cost increases, and a continual rise in such costs could adversely affect consumer spending and demand for our products and increase our operating costs, both of which could adversely affect our business, financial condition and operating results.

***Our future success is dependent on our ability to execute our business strategy effectively and deliver value to our customers.***

We believe our future success will depend on our ability to execute our business strategy effectively and deliver value to our customers. We believe that our breadth of product assortment across a variety of hard surface flooring categories, low prices, and in-store availability of the products we offer in project-ready quantities, as well as the quality of our products and customer service, are among the key competitive advantages and important elements of our total value proposition. If we are unsuccessful in staying competitive with our current value proposition, the demand for our products would decrease, and customers may decide to purchase products from our competitors instead of us. If this were to occur, our net sales, market share and operating results would be adversely affected.

***Our operating results may be adversely affected if we are not successful in managing our inventory.***

We currently maintain a high level of inventory consisting of on average approximately 3,800 SKUs per store and an average inventory per store of approximately \$2.5 million at cost in order to have a broad assortment of products across a wide variety of hard surface flooring categories in project-ready quantities. We also carry an additional \$156.9 million of inventory outside our stores, primarily at our distribution centers, as of the end of fiscal 2018. The investment associated with this high level of inventory is substantial, and efficient inventory management is a key component of our business success and profitability. If we fail to adequately project the amount or mix of our inventory, we may miss sales opportunities or have to take unanticipated markdowns or hold additional clearance events to dispose of excess inventory, which will adversely affect our operating results.

In the past, we have incurred costs associated with inventory markdowns and obsolescence. Due to the likelihood that we will continue to incur such costs in the future, we generally include an allowance for such costs in our projections. However, the costs that we actually incur may be substantially higher than our estimate and adversely affect our operating results.

We continue to focus on ways to reduce these risks, but we cannot assure you that we will be successful in our inventory management.

***Our operating results may be adversely affected by inventory shrinkage and damage.***

We are subject to the risk of inventory shrinkage and damage, including the damage or destruction of our inventory by natural disasters or other causes. We have experienced charges in the past, and we cannot assure you that the measures we are taking will effectively address the problem of inventory shrinkage and damage in the future. Although some level of inventory shrinkage and damage is an unavoidable cost of doing business, we could experience higher-than-normal rates of inventory shrinkage and damage or incur increased security and other costs to combat inventory theft and damage. If we are not successful in managing our inventory balances, our operating results may be adversely affected.

***If we are unable to enter into leases for additional stores on acceptable terms or renew or replace our current store leases, or if one or more of our current leases is terminated prior to expiration of its stated term, and we cannot find suitable alternate locations, our growth and profitability could be adversely affected.***

We currently lease all of our store locations and our store support center. Our growth strategy largely depends on our ability to identify and open future store locations, which can be difficult because our stores generally require at least 50,000 square feet of floor space. Our ability to negotiate acceptable lease terms for these store locations, to re-negotiate acceptable terms on expiring leases or to negotiate acceptable terms for suitable alternate locations could depend on conditions in the real estate market, competition for desirable properties, our relationships with current and prospective landlords, or on other factors that are not within our control. Any or all of these factors and conditions could adversely affect our growth and profitability.

***We intend to move our existing headquarters and may face disruption and additional costs.***

Due to space constraints at our existing store support center, which serves as our corporate headquarters, we have entered into a lease to relocate our corporate headquarters and expect to begin moving to the new store support center in the third quarter of fiscal 2019. In connection with the relocation, we expect to incur additional expenses, including those related to moving and exit costs and tenant improvements, as well as furniture and equipment for the new corporate headquarters. The relocation could result in business disruption and could have a negative impact on our operating results. In addition, we may incur charges related to exiting our current store support center if we are not able to exit or release on favorable terms.

***Our net sales growth could be adversely affected if comparable store sales growth is less than we expect.***

While future net sales growth will depend substantially on our plans for new store openings, our comparable store sales growth is a significant driver of our net sales, profitability and overall business results. Because numerous factors affect our comparable store sales growth, including, among others, economic conditions, the retail sales environment, the home improvement spending environment, housing turnover, housing appreciation, interest rates, the hard surface flooring industry and the impact of competition, the ability of our customers to obtain credit, changes in our product mix, the in-stock availability of products that are in demand, changes in staffing at our stores, cannibalization resulting from the opening of new stores in existing markets, greater

cannibalization than we modeled for new stores, lower than expected ramp-up in new store net sales, changes in advertising and other operating costs, weather conditions, retail trends and our overall ability to execute our business strategy and planned growth effectively, it is possible that we will not achieve our targeted comparable store sales growth or that the change in comparable store sales could be negative. If this were to happen, it is likely that overall net sales growth would be adversely affected.

***If we fail to identify and maintain relationships with a sufficient number of suppliers, our ability to obtain products that meet our high quality standards at attractive prices could be adversely affected.***

We purchase flooring and other products directly from suppliers located around the world. We do not have long-term contractual supply agreements with our suppliers that obligate them to supply us with products exclusively or at specified quantities or prices. As a result, our current suppliers may decide to sell products to our competitors and may not continue selling products to us. In order to retain the competitive advantage that we believe results from these relationships, we need to continue to identify, develop and maintain relationships with qualified suppliers that can satisfy our high standards for quality and safety and our requirements for delivery of flooring and other products in a timely and efficient manner at attractive prices. The need to develop new relationships will be particularly important as we seek to expand our operations and enhance our product offerings in the future. The loss of one or more of our existing suppliers or our inability to develop relationships with new suppliers could reduce our competitiveness, slow our plans for further expansion and cause our net sales and operating results to be adversely affected.

***We will require significant capital to fund our expanding business, which may not be available to us on satisfactory terms or at all. If we are unable to maintain sufficient levels of cash flow or if we do not have sufficient availability under the ABL Facility, we may not meet our growth expectations or we may require additional financing, which could adversely affect our financial health and impose covenants that limit our business activities.***

We plan to continue investing for growth, including opening new stores, remodeling existing stores, adding staff, adding distribution center capacity and upgrading our information technology systems and other infrastructure. These investments will require significant capital, which we plan on funding with cash flow from operations and borrowings under the ABL Facility (as defined below).

If our business does not generate sufficient cash flow from operations to fund these activities or if these investments do not yield cash flows in line with past performance or our expectations, we may need additional equity or debt financing. If such financing is not available to us, or is not available on satisfactory terms, our ability to operate and expand our business or respond to competitive pressures would be curtailed, and we may need to delay, limit or eliminate planned store openings or operations or other elements of our growth strategy. If we raise additional capital by issuing equity securities or securities convertible into equity securities, our stockholders' ownership would be diluted.

***We depend on a number of suppliers, and any failure by any of them to supply us with quality products on attractive terms and prices may adversely affect our business, financial condition and operating results.***

We depend on our suppliers to deliver quality products to us on a timely basis at attractive prices. Additionally, we source the products that we sell from over 240 domestic and international suppliers. However, in the future, we may not be able to acquire desired merchandise in sufficient quantities on terms acceptable to us, which may impair our relationship with our customers, impair our ability to attract new customers, reduce our competitiveness and adversely affect our business, financial condition and operating results.

***Changes in tax laws, trade policies and regulations or in our operations and newly enacted laws or regulations may impact our effective tax rate or may adversely affect our business, financial condition and operating results.***

Changes in tax laws in any of the multiple jurisdictions in which we operate, or adverse outcomes from tax audits that we may be subject to in any of the jurisdictions in which we operate, could result in an unfavorable change in our effective tax rate, which could adversely affect our business, financial condition and operating results.

Developments in tax policy or trade relations could have a material adverse effect on our business, results of operations and liquidity. If there are any adverse changes in tax laws or trade policies that result in an increase in our costs, we may not be able to



adjust the prices of our products, especially in the short-term, to recover such costs, and a rise in such costs could adversely affect our business, financial condition and operating results.

***The failure of our suppliers to adhere to the quality standards that we set for our products could lead to investigations, litigation, write-offs, recalls or boycotts of our products, which could damage our reputation and our brand, increase our costs, and otherwise adversely affect our business.***

We do not control the operations of our suppliers. Although we conduct initial due diligence prior to engaging our suppliers and require our suppliers to certify compliance with applicable laws and regulations, we cannot guarantee that our suppliers will comply with applicable laws and regulations or operate in a legal, ethical and responsible manner. Additionally, it is possible that we may not be able to identify noncompliance by our suppliers notwithstanding these precautionary measures. Violation of applicable laws and regulations by our suppliers or their failure to operate in a legal, ethical or responsible manner, could expose us to legal risks, cause us to violate laws and regulations and reduce demand for our products if, as a result of such violation or failure, we attract negative publicity. In addition, the failure of our suppliers to adhere to the quality standards that we set for our products could lead to government investigations, litigation, write-offs and recalls, which could damage our reputation and our brand, increase our costs, and otherwise adversely affect our business.

***We procure the majority of our products from suppliers located outside of the United States, and as a result, we are subject to risks associated with obtaining products from abroad that could adversely affect our business, financial condition and results of operations.***

We procure the majority of our products from suppliers located outside of the United States. As a result, we are subject to risks associated with obtaining products from abroad, including:

- political unrest, acts of war, terrorism and economic instability resulting in the disruption of trade from foreign countries where our products originate;
- currency exchange fluctuations;
- the imposition of new or more stringent laws and regulations, including those relating to environmental, health and safety matters and climate change issues, labor conditions, quality and safety standards, trade restrictions and restrictions on funds transfers;
- the imposition of new or different duties (including antidumping and countervailing duties), tariffs, taxes and/or other charges on exports or imports, including as a result of errors in the classification of products upon entry or changes in the interpretation or application of rates or regulations relating to the import or export of our products;
- the risk that one or more of our suppliers will not adhere to applicable legal requirements, including fair labor standards, the prohibition on child labor, environmental, product safety or manufacturing safety standards, anti-bribery and anti-kickback laws such as the Foreign Corrupt Practices Act (the “FCPA”) and sourcing laws such as the Lacey Act;
- disruptions or delays in production, shipments, delivery or processing through ports of entry (including those resulting from strikes, lockouts, work-stoppages or slowdowns, or other forms of labor unrest);
- changes in local economic conditions in countries where our suppliers are located; and
- differences in product standards, acceptable business practice and legal environments.

Additionally, we import approximately 50% of the products we sell from China. The Chinese government has in the past imposed restrictions on manufacturing facilities, including a shut-down of transportation of materials and power plants to reduce air pollution. If, in the future, restrictions are imposed that include our operations, our suppliers’ ability to supply current or new orders would be significantly impacted. These and other factors beyond our control could disrupt the ability of our suppliers to ship certain products to us cost-effectively or at all, expose us to significant operational and legal risk and negatively affect our reputation, any of which could adversely affect our business, financial condition and results of operations.

***Our ability to offer compelling products, particularly products made of more exotic species or unique stone, depends on the continued availability of sufficient suitable natural products.***

Our business strategy depends on offering a wide assortment of compelling products to our customers. We sell, among other things, flooring made from various wood species and natural stone from quarries throughout the world. Our ability to obtain an adequate volume and quality of hard-to-find products depends on our suppliers' ability to furnish those products, which, in turn, could be affected by many things, including events such as forest fires, insect infestation, tree diseases, prolonged drought, other adverse weather and climate conditions and the exhaustion of stone quarries. Government regulations relating to forest management practices also affect our suppliers' ability to harvest or export timber and other products, and changes to regulations and forest management policies, or the implementation of new laws or regulations, could impede their ability to do so. If our suppliers cannot deliver sufficient products, and we cannot find replacement suppliers, our net sales and operating results may be adversely affected.

***Our business exposes us to personal injury, product liability and warranty claims and related governmental investigations, which could result in negative publicity, harm our brand and adversely affect our business, financial condition and operating results.***

Our stores and distribution centers are warehouse environments that involve the operation of forklifts and other machinery and the storage and movement of heavy merchandise, all of which are activities that have the inherent danger of injury or death to employees or customers despite safety precautions, training and compliance with federal, state and local health and safety regulations. While we have insurance coverage in place in addition to policies and procedures designed to minimize these risks, we may nonetheless be unable to avoid material liabilities for an injury or death arising out of these activities.

In addition, we face an inherent risk of exposure to product liability or warranty claims or governmental investigations in the event that the use of our products is alleged to have resulted in economic loss, personal injury or property damage or violated environmental or other laws. If any of our products proves to be defective or otherwise in violation of applicable law, we may be required to recall or redesign such products. Further, in such instances, we may be subject to legal action. We generally seek contractual indemnification from our suppliers. However, such contractual indemnification may not be enforceable against the supplier, particularly because many of our suppliers are located outside of the United States. Any personal injury, product liability or warranty claim made against us, whether or not it has merit, or governmental investigation related to our products, could be time-consuming and costly to defend or respond to, may not be covered by insurance carried by us, could result in negative publicity, could harm our brand and could adversely affect our business, financial condition and operating results. In addition, any negative publicity involving our suppliers, employees, and other parties who are not within our control could adversely affect us.

***Unfavorable allegations, government investigations and legal actions surrounding our products and us could harm our reputation, impair our ability to grow or sustain our business, and adversely affect our business, financial condition and operating results.***

We rely on our reputation for offering great value, superior service and a broad assortment of high-quality, safe products. If we become subject to unfavorable allegations, government investigations or legal actions involving our products or us, such circumstances could harm our reputation and our brand and adversely affect our business, financial condition and operating results. If this negative impact is significant, our ability to grow or sustain our business could be jeopardized.

For instance, we have previously settled claims related to unfavorable allegations surrounding the product quality of our laminates sourced from China. Although such claims have been resolved, we cannot predict whether we will face additional lawsuits that are not covered by the settlement or the release. If additional lawsuits are filed, we could incur significant costs, be liable to damages, be subject to fines, penalties, injunctive relief, criminal charges or other legal risks, which could reduce demand for our products and adversely affect our business, financial condition and operating results.

Negative publicity surrounding product matters, including publicity about other retailers, may harm our reputation and affect the demand for our products. In addition, if more stringent laws or regulations are adopted in the future, we may have difficulty complying with the new requirements imposed by such laws and regulations, and in turn, our business, financial condition and operating results could be adversely affected. Moreover, regardless of whether any such changes are adopted, we may become subject to claims or governmental investigations alleging violations of applicable laws and regulations. Any such matter may subject us to fines, penalties, injunctions, litigation and/or potential criminal violations. Any one of these results could negatively affect our business, financial condition and operating results and impair our ability to grow or sustain our business.

***If we violate or are alleged to have violated environmental, health and safety laws and regulations, we could incur significant costs and other negative effects that could reduce demand for our products and adversely affect our business, financial condition and operating results.***

Certain portions of our operations are subject to laws and regulations governing the environmental protection of natural resources and health and safety, including formaldehyde emissions and the use, storage, handling, generation, transportation, treatment, emission, release, discharge and disposal of certain hazardous materials and wastes. In addition, certain of our products are subject to laws and regulations relating to the importation, exportation, acquisition or sale of certain plants and plant products, including those that have been illegally harvested, and the emissions of hazardous materials.

We operate our business in accordance with standards and procedures designed to comply with the applicable laws and regulations in these areas and work closely with our suppliers in order to comply with such laws and regulations. If we violate or are alleged to have violated these laws, we could incur significant costs, be liable for damages, experience delays in shipments of our products, be subject to fines, penalties, criminal charges or other legal risks, or suffer reputational harm, any of which could reduce demand for our products and adversely affect our business, financial condition and operating results. In addition, there can be no assurance that such laws or regulations 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 or regulations.

***We are engaged in various legal actions, claims and proceedings arising in the ordinary course of business and, while we cannot predict the outcomes of such proceedings and other contingencies with certainty, this litigation and any potential future litigation could have an adverse impact on us.***

We are engaged in various legal actions, claims and proceedings arising in the ordinary course of business, including claims related to breach of contract, product liabilities, intellectual property matters and employment related matters resulting from our business activities. As with most actions such as these, an estimate of any possible and/or ultimate liability cannot always be determined. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors. Additionally, we cannot guarantee that we will not become engaged in additional legal actions, claims, proceedings or governmental investigations in the future. Any such action could result in negative publicity, harm to our reputation and adversely affect our business, financial condition and operating results.

***Labor activities could cause labor relations difficulties for us.***

Currently none of our employees are represented by a union; however, our employees have the right at any time to form or affiliate with a union. As we continue to grow, enter different regions and operate distribution centers, unions may attempt to organize all or part of our employee base at certain stores or distribution centers within certain regions. We cannot predict the adverse effects that any future organizational activities will have on our business, financial condition and operating results. If we were to become subject to work stoppages, we could experience disruption in our operations and increases in our labor costs, either of which could adversely affect our business, financial condition and operating results.

***Federal, state or local laws and regulations, or our failure to comply with such laws and regulations, could increase our expenses, restrict our ability to conduct our business and expose us to legal risks.***

We are subject to a wide range of general and industry-specific laws and regulations imposed by federal, state and local authorities in the countries in which we operate including those related to customs, foreign operations (such as the FCPA), truth-in-advertising, consumer protection (such as the Telephone Consumer Protection Act), privacy, product safety (such as the Formaldehyde Standards in Composite Wood Products Act), the environment (such as the Lacey Act), intellectual property infringement, zoning and occupancy matters as well as the operation of retail stores and distribution facilities. In addition, various federal and state laws govern our relationship with, and other matters pertaining to, our employees, including wage and hour laws, laws governing independent contractor classifications, requirements to provide meal and rest periods or other benefits, family leave mandates, requirements regarding working conditions and accommodations to certain employees, citizenship or work authorization and related requirements, insurance and workers' compensation rules and anti-discrimination laws. In recent years, we and other parties in the flooring industry have been or currently are parties to litigation involving claims that allege violations of the foregoing laws, including claims related to product safety and patent claims. In addition, there has been an increase in the number of wage and hour class action claims that allege misclassification of overtime eligible workers and/or failure to pay overtime-eligible workers for

all hours worked, particularly in the retail industry. Although we believe that we have complied with these laws and regulations, there is nevertheless a risk that we will become subject to claims that allege we have failed to do so. Any claim that alleges a failure by us to comply with any of the foregoing laws and regulations may subject us to fines, penalties, injunctions, litigation and/or potential criminal violations, which could adversely affect our reputation, business, financial condition and operating results.

Certain of our products may require us to spend significant time and resources in order to comply with applicable advertising, labeling, importation, exportation, environmental, health and safety laws and regulations because if we violate these laws or regulations, we could experience delays in shipments of our goods, be subject to fines or penalties, be liable for costs and damages or suffer reputational harm, any of which could reduce demand for our merchandise and adversely affect our business, financial condition and operating results.

Any changes to the foregoing laws or regulations or any new laws or regulations that are passed or go into effect may make it more difficult for us to operate our business and in turn adversely affect our operating results.

We may also be subject to audits by various taxing authorities. Similarly, changes in tax laws in any of the multiple jurisdictions in which we operate, or adverse outcomes from tax audits that we may be subject to in any of the jurisdictions in which we operate, could result in an unfavorable change in our effective tax rate, which could adversely affect our business, financial condition and operating results. In addition, given the nature of our business, certain of our sales are exempt from state sales taxes. If we are audited and fail to maintain proper documentation, any adjustments resulting from such audits could increase our tax liability, including any interest or penalties.

***If our efforts to protect the privacy and security of information related to our customers, us, our employees, our suppliers and other third parties are not successful, we could become subject to litigation, investigations, liability and negative publicity that could significantly harm our reputation and relationships with our customers and adversely affect our business, financial condition and operating results.***

Our business, like that of most retailers, involves the receipt, storage and transmission of customers' personal information, consumer preferences and payment card data, as well as other confidential information related to us, our employees, our suppliers and other third parties, some of which is entrusted to third-party service providers and vendors that provide us with technology, systems and services that we use in connection with the receipt, storage and transmission of such information. Techniques used for cyber attacks designed to gain unauthorized access to these types of sensitive information by breaching or sabotaging critical systems of large organizations are constantly evolving and generally are difficult to recognize and react to effectively. We may be unable to anticipate these techniques or to implement adequate preventive or reactive security measures. Notwithstanding widespread recognition of the cyber attack threat and improved data protection methods, high profile electronic security breaches leading to unauthorized release of sensitive information have occurred in recent years with increasing frequency at a number of major U.S. companies, including several large retailers, notwithstanding widespread recognition of the cyber attack threat and improved data protection methods.

Despite our security measures and those of third parties with whom we do business, such as our banks, merchant card processing and other technology vendors, our respective systems and facilities may be vulnerable to criminal cyber-attacks or security incidents due to malfeasance, intentional or inadvertent security breaches by employees, or other vulnerabilities such as defects in design or manufacture. Unauthorized parties may also attempt to gain access to our systems or facilities through fraud, trickery or other forms of deception targeted at our customers, employees, suppliers and service providers. Any such incidents could compromise our networks and the information stored there could be accessed, misused, publicly disclosed, lost or stolen.

As noted above, the techniques used by criminals to obtain unauthorized access to sensitive data change frequently and often are not recognized until launched against a target; accordingly, we may be unable to anticipate these techniques or implement adequate preventative measures. In addition, advances in computer capabilities, new technological discoveries or other developments may also compromise or result in the obsolescence of the technology used to protect sensitive information. An actual or anticipated attack or security incident may cause us to incur additional costs, including costs related to diverting or deploying personnel, implementing preventative measures, training employees and engaging third-party experts and consultants. Further, any security breach incident could expose us to risks of data loss, regulatory and law enforcement investigations, litigation and liability and could seriously disrupt our operations and any resulting negative publicity could significantly harm our reputation and relationships with our customers and adversely affect our business, financial condition and operating results.

***A material disruption in our information systems, including our website and call center, could adversely affect our business or operating results and lead to reduced net sales and reputational damage.***

We rely on our information systems to process transactions, summarize our results of operations and manage our business. In particular, our website and our call center are important parts of our integrated connected customer strategy and customers use these systems as information sources on the range of products available to them and as a way to order our products. Therefore, the reliability and capacity of our information systems is critical to our operations and the implementation of our growth initiatives. However, our information systems are subject to damage or interruption from planned upgrades in technology interfaces, power outages, computer and telecommunications failures, computer viruses, cyber-attacks or other security breaches and catastrophic events such as fires, floods, earthquakes, tornadoes, hurricanes, acts of war or terrorism and usage errors by our employees. If our information systems are damaged or cease to function properly, we may have to make a significant investment to fix or replace them, and we may suffer losses of critical data and/or interruptions or delays in our operations. In addition, to keep pace with changing technology, we must continuously implement new information technology systems as well as enhance our existing systems. Moreover, the successful execution of some of our growth strategies, in particular the expansion of our connected customer and online capabilities, is dependent on the design and implementation of new systems and technologies and/or the enhancement of existing systems. Any material disruption in our information systems, or delays or difficulties in implementing or integrating new systems or enhancing or expanding current systems, could have an adverse effect on our business (in particular our call center and online operations) and our operating results and could lead to reduced net sales and reputational damage.

***We identified a material weakness in our internal controls related to ineffective information technology general controls which, if not remediated appropriately or timely, could result in loss of investor confidence and adversely impact our stock price.***

Internal controls related to the operation of technology systems are critical to maintaining adequate internal control over financial reporting. As disclosed in Part II, Item 9A, during the fourth quarter of fiscal 2018, management identified a material weakness in internal controls related to ineffective information technology general controls (“ITGCs”) in the areas of user access and program change-management over certain information technology systems that support the Company’s financial reporting processes. As a result, management concluded that our internal control over financial reporting was not effective as of December 27, 2018.

Although we are in the process of carrying out remediation activities, we cannot provide any assurance that the measures we have taken to date, together with any measures we may take in the future, will be sufficient to remediate the material weakness in our internal control over financial reporting or to avoid potential future material weaknesses. These measures will result in additional technology and other expenses. If we are unable to remediate the material weakness, or are otherwise unable to maintain effective internal control over financial reporting or disclosure controls and procedures, our ability to record, process and report financial information accurately, and to prepare financial statements within required time periods, could be adversely affected. This could subject us to litigation or investigations requiring management resources and payment of legal and other expenses and could result in negative publicity, harm to our reputation and adversely affect our business, financial condition and operating results or adversely affect the market price of our common stock.

***We are subject to payments-related risks that could increase our operating costs, expose us to fraud, subject us to potential liability and potentially disrupt our business.***

We accept payments using a variety of methods, including credit cards, debit cards, gift cards and physical bank checks. These payment options subject us to many compliance requirements, including, but not limited to, compliance with the Payment Card Industry Data Security Standards, which represents a common set of industry tools and measurements to help ensure the safe handling of sensitive information, and compliance with contracts with our third-party processors. These payment options also subject us to potential fraud by criminal elements seeking to discover and take advantage of security vulnerabilities that may exist in some of these payment systems. For certain payment methods, including credit cards and debit cards, we pay interchange and other fees, which may increase over time and raise our operating costs and lower profitability. We rely on third parties to provide payment processing services, including the processing of credit cards, debit cards and gift cards, and it could disrupt or harm our business if these companies become unwilling or unable to provide these services to us, experience a data security incident or fail to comply with applicable rules and industry standards. We are also subject to payment card association operating rules, including data security rules, certification requirements, and rules governing electronic funds transfers, which could change or be reinterpreted to make it difficult or impossible for us to comply. If we fail to comply with these rules or requirements, or if our data security systems or payment card information of our customers are breached or compromised, there is the potential that parties could seek damages from us, we may be liable for card issuing banks’ costs, subject to fines and higher transaction fees, and lose our ability to accept credit cards and debit

card payments from our customers, process electronic funds transfers, or facilitate other types of online payments, we could lose the confidence of customers and our business, financial condition and operating results could be adversely affected. We may also need to expend significant management and financial resources to become or remain compliant with relevant standards and requirements, which could divert resources from other initiatives and adversely affect our business, financial condition and operating results.

***Our facilities and systems, as well as those of our suppliers, are vulnerable to natural disasters and other unexpected events, and as a result we may lose merchandise and be unable to effectively deliver it to our stores.***

Our retail stores, store support center and distribution centers, as well as the operations of our suppliers from which we receive goods and services, are vulnerable to damage from earthquakes, tornadoes, hurricanes, fires, floods and similar events. If any of these events result in damage to our facilities, systems or equipment, or those of our suppliers, they could adversely affect our ability to stock our stores and deliver products to our customers, and could adversely affect our net sales and operating results. In addition, we may incur costs in repairing any damage beyond our applicable insurance coverage. In particular, any disruption to any of our distribution centers could have a material adverse impact on our business.

***Material damage to, or interruptions in, our information systems as a result of external factors, staffing shortages and difficulties in updating our existing software or developing or implementing new software could adversely affect our business, financial condition and operating results.***

We depend largely upon our information technology systems in the conduct of all aspects of our operations. Such systems are subject to damage or interruption from power outages, computer and telecommunications failures, computer viruses and security breaches. Damage or interruption to our information systems may require a significant investment to fix or replace them, and we may suffer interruptions in our operations in the interim including issues operating our distribution centers and/or managing our inventory. In addition, costs and potential problems and interruptions associated with the implementation of new or upgraded systems and technology, or with maintenance or adequate support of existing systems, could also disrupt or reduce the efficiency of our operations. Further, the software programs supporting many of our systems were licensed to us by independent software developers. The inability of these developers or us to continue to maintain and upgrade these information systems and software programs would disrupt or reduce the efficiency of our operations if we were unable to convert to alternate systems in an efficient and timely manner and could adversely affect our business, financial condition and operating results. Moreover, any material interruptions or failures in our information systems may adversely affect our business, financial condition and operating results.

***As we have a high concentration of stores in the southern region of the United States, we are subject to regional risks.***

We have a high concentration of stores in the southern region of the United States. If this market suffers an economic downturn or other significant adverse event, our comparable store sales, net sales, profitability and the ability to implement our planned expansion could be adversely affected. Any natural disaster, extended adverse weather or other serious disruption in this market, whether due to fire, tornado, hurricane, or any other calamity, could damage inventory and could result in decreased net sales.

***Our success depends substantially upon the continued retention of our key personnel, which we consider to be our executive officers.***

We believe that our success has depended and continues to depend to a significant extent on the efforts and abilities of our key personnel, which we consider to be our executive officers. We have employment agreements with each of our executive officers. Our failure to retain members of that team could impede our ability to build on the efforts they have undertaken with respect to our business.

***We do not maintain “key man” life insurance policies on our key personnel.***

We do not have “key man” life insurance policies for any of our key personnel. If we were to obtain “key man” insurance for our key personnel, there can be no assurance that the amounts of such policies would be sufficient to pay losses experienced by us as a result of the loss of any of those personnel.

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

Our success depends in part on our ability to attract, hire, train and retain qualified managers and staff. Purchasing hard surface flooring is an infrequent event for BIY and DIY consumers, and the typical consumer in these groups has little knowledge of the range, characteristics and suitability of the products available before starting the purchasing process. Therefore, consumers in the hard surface flooring market expect to have sales associates serving them who are knowledgeable about the entire assortment of products offered by the retailer and the process of choosing and installing hard surface flooring.

Each of our stores is managed by a store manager who has the flexibility (with the support of regional managers) to use his or her knowledge of local market dynamics to customize each store in a way that is most likely to increase net sales and profitability. Our store managers are also expected to anticipate, gauge and quickly respond to changing consumer demands in these markets. Further, it generally takes a substantial amount of time for our store managers to develop the entrepreneurial skills that we expect them to have in order to make our stores successful.

There is a high level of competition for qualified regional managers, store managers and sales associates among home improvement and flooring retailers in local markets, and as a result, we may not succeed in attracting and retaining the personnel we require to conduct our current operations and support our plans for expansion. In addition, we compete with other retail businesses for many of our associates in hourly positions, and we invest significant resources in training and motivating them to maintain a high level of job satisfaction. These positions have historically had high turnover rates, which can lead to increased training and retention costs, particularly in a tight labor market. If our recruiting and retention efforts are not successful, we may have a shortage of qualified employees in future periods. Any such shortage would decrease our ability to effectively serve our customers. Such a shortage would also likely lead to higher wages for employees and a corresponding reduction in our operating results. In addition, as we expand into new markets, we may find it more difficult to hire, develop and retain qualified employees and may experience increased labor costs. Any failure by us to attract, train and retain highly qualified managers and staff could adversely affect our operating results and future growth opportunities.

***The effectiveness of our advertising strategy is a driver of our future success.***

We believe that our growth was in part a result of our successful investment in local advertising. As we enter new markets that often have more expensive advertising rates, we may need to increase our advertising expenses to broaden the reach and frequency of our advertising to increase the recognition of our brand. If our advertisements fail to draw customers in the future, or if the cost of advertising or other marketing materials increases significantly, we could experience declines in our net sales and operating results.

***Our intellectual property rights are valuable, and any failure to protect them could reduce the value of our products and brand and harm our business.***

We regard our intellectual property as having significant value, and our brand is an important factor in the marketing of our products. However, we cannot assure you that the steps we take to protect our trademarks or intellectual property will be adequate to prevent others from copying or using our trademarks or intellectual property without authorization. If our trademarks or intellectual property are copied or used without authorization, the value of our brand, its reputation, our competitive advantages and our goodwill could be harmed.

***We may be involved in disputes from time to time relating to our intellectual property and the intellectual property of third parties.***

We may become parties to disputes from time to time over rights and obligations concerning intellectual property, and we may not prevail in these disputes. Third parties may raise claims against us alleging infringement or violation of the intellectual property of such third-party. Even if we prevail in such disputes, the costs we incur in defending such dispute may be material and costly. Some third-party intellectual property rights may be extremely broad, and it may not be possible for us to conduct our operations in such a way as to avoid violating any such intellectual property rights. Any such intellectual property claim could subject us to costly litigation and impose a significant strain on our financial resources and management personnel regardless of whether such claim has merit. The liability insurance we maintain may not adequately cover potential claims of this type, and we may be required to pay monetary damages or license fees to third parties, which could have a material adverse effect on our business, financial condition and operating results.

***Our ability to control higher health care costs is limited and could adversely affect our business, financial condition and operating results.***

With the passage in 2010 of the U.S. Patient Protection and Affordable Care Act (as amended, the “Affordable Care Act”), we are required to provide affordable coverage, as defined in the Affordable Care Act, to all employees, or otherwise be subject to a payment per employee based on the affordability criteria in the Affordable Care Act. Additionally, some states and localities have passed state and local laws mandating the provision of certain levels of health benefits by some employers. These requirements limit our ability to control employee health care costs.

Efforts to modify, repeal or otherwise invalidate all, or certain provisions of, the Affordable Care Act and/or adopt a replacement healthcare reform law may impact our employee healthcare costs. At this time, there is uncertainty concerning whether the Affordable Care Act will be repealed or what requirements will be included in a new law, if enacted. If health care costs rise, we may experience increased operating costs, which may adversely affect our business, financial condition and operating results.

***We are a holding company with no business operations of our own and depend on cash flow from our subsidiaries to meet our obligations.***

We are a holding company with no business operations of our own or material assets other than the equity of our subsidiaries. All of our operations are conducted by our subsidiaries. As a holding company, we will require dividends and other payments from our subsidiaries to meet cash requirements.

The terms of our \$300 million asset-based revolving credit facility (the “ABL Facility”), and our \$350 million senior secured term loan facility (the “Term Loan Facility” and together with the ABL Facility, our “Credit Facilities”), restrict our subsidiaries from paying dividends and otherwise transferring cash or other assets to us except in certain limited circumstances. If we become insolvent or there is a liquidation or other reorganization of any of our subsidiaries, our stockholders likely will have no right to proceed against their assets. Creditors of those subsidiaries will be entitled to payment in full from the sale or other disposal of the assets of those subsidiaries before we, as an equity holder, would be entitled to receive any distribution from that sale or disposal. If our subsidiaries are unable to pay dividends or make other payments to us when needed, we will be unable to satisfy our obligations.

***We face risks related to our indebtedness.***

As of December 27, 2018, the principal amount of our total indebtedness was approximately \$145.3 million related to our indebtedness outstanding under the Term Loan Facility. In addition, as of December 27, 2018, we had the ability to access approximately \$289.2 million of unused borrowings available under the ABL Facility without violating any covenants thereunder and had approximately \$10.9 million in outstanding letters of credit thereunder.

Our indebtedness, combined with our lease and other financial obligations and contractual commitments, could adversely affect our business, financial condition and operating results by:

- making it more difficult for us to satisfy our obligations with respect to our indebtedness, including restrictive covenants and borrowing conditions, which may lead to an event of default under the agreements governing our debt;
- making us more vulnerable to adverse changes in general economic, industry and competitive conditions and government regulation;
- requiring us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of cash flows to fund current operations and future growth;
- exposing us to the risk of increased interest rates as our borrowings under our Credit Facilities are at variable rates;
- restricting us from making strategic acquisitions or causing us to make non-strategic divestitures;



- requiring us to comply with financial and operational covenants, restricting us, among other things, from placing liens on our assets, making investments, incurring debt, making payments to our equity or debt holders and engaging in transactions with affiliates;
- limiting our ability to borrow additional amounts for working capital, capital expenditures, acquisitions, debt service requirements, execution of our business and growth strategies or other purposes; and
- limiting our ability to obtain credit from our suppliers and other financing sources on acceptable terms or at all.

We may also incur substantial additional indebtedness in the future, subject to the restrictions contained in our Credit Facilities. If such new indebtedness is in an amount greater than our current debt levels, the related risks that we now face could intensify. However, we cannot assure you that any such additional financing will be available to us on acceptable terms or at all. Moreover, for taxable years beginning after December 31, 2017, the deductibility of net business interest expenses on our indebtedness for each taxable year could be limited under the Tax Cuts and Jobs Act (the “Act”).

***Significant amounts of cash are required to service our indebtedness and operating lease obligations, and any failure to meet our debt service obligations could adversely affect our business, financial condition and operating results.***

Our ability to pay interest on and principal of our debt obligations will primarily depend upon our future operating performance. As a result, prevailing economic conditions and financial, business and other factors, many of which are beyond our control, will affect our ability to make these payments.

If we do not generate sufficient cash flow from operations to satisfy our debt service obligations, we may have to undertake alternative financing plans, such as refinancing or restructuring our indebtedness, selling our assets, reducing or delaying capital investments or seeking to raise additional capital. Our ability to restructure or refinance our debt will depend on the condition of the capital markets and our financial condition at such time. Any refinancing of our debt could be at higher interest rates and may require us to comply with more onerous covenants, which could further restrict our business operations. The terms of existing or future debt instruments may restrict us from adopting some of these alternatives. In addition, any failure to make payments of interest and principal on our outstanding indebtedness on a timely basis would likely result in a reduction of our credit rating, which could harm our ability to incur additional indebtedness on acceptable terms. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Our Credit Facilities—” for more information.

Our inability to generate sufficient cash flow to satisfy our debt obligations, or to refinance our obligations at all or on acceptable terms, could have an adverse effect on our business, financial condition and operating results.

We cannot assure you that our business will generate sufficient cash flow from operations or that future borrowings will be available to us in amounts sufficient to enable us to make payments on our indebtedness or to fund our operations.

***Our debt agreements contain restrictions that may limit our flexibility in operating our business.***

We are a holding company, and accordingly, substantially all of our operations are conducted through our subsidiaries. The credit agreements governing our Credit Facilities contain, and any future indebtedness would likely contain, a number of restrictive covenants that impose significant operating and financial restrictions, including restrictions on our ability to engage in acts that may be in our best long-term interests. The credit agreements governing our Credit Facilities include covenants that, among other things, restrict our and our subsidiaries’ ability to:

- incur additional indebtedness;
- create liens;
- make investments, loans or advances;
- merge or consolidate;

- sell assets, including capital stock of subsidiaries or make acquisitions;
- pay dividends on capital stock or redeem, repurchase or retire capital stock or make other restricted payments;
- enter into transactions with affiliates;
- repurchase certain indebtedness; and
- exceed a certain total net leverage ratio or, in certain cases, maintain less than a certain fixed charge coverage ratio.

Based on the foregoing factors, the operating and financial restrictions and covenants in our current debt agreements and any future financing agreements could adversely affect our ability to finance future operations or capital needs or to engage in other business activities.

In addition, a breach of any of the restrictive covenants in our Credit Facilities may constitute an event of default, permitting the lenders to declare all outstanding indebtedness under both our Credit Facilities to be immediately due and payable or to enforce their security interest, which could adversely affect our ability to respond to changes in our business and manage our operations. Upon the occurrence of an event of default under any of the agreements governing our Credit Facilities, the lenders could elect to declare all amounts outstanding to be due and payable and exercise other remedies as set forth in such credit agreements. If any of our indebtedness under either of our Credit Facilities were to be accelerated, there can be no assurance that our assets would be sufficient to repay this indebtedness in full, which could adversely affect our ability to continue to operate as a going concern. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Our Credit Facilities” for more information.

***Our fixed lease obligations could adversely affect our operating results.***

We are required to use a significant portion of cash generated by our operations to satisfy our fixed lease obligations, which could adversely affect our ability to obtain future financing to support our growth or other operational investments. We will require substantial cash flows from operations to make our payments under our operating leases, all of which provide for periodic increases in rent. As of December 27, 2018, our minimum annual rental obligations under long-term operating leases for the fiscal years ending December 26, 2019 and December 31, 2020 are approximately \$114.1 million and \$131.4 million, respectively. If we are not able to make payments under our operating leases, this could trigger defaults under other leases or, in certain circumstances, under our Credit Facilities, which could cause the counterparties or lenders under those agreements to accelerate the obligations due thereunder.

***Changes to accounting rules or regulations could adversely affect our operating results.***

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States (“GAAP”). New accounting rules or regulations and changes to existing accounting rules or regulations have occurred and may occur in the future. Future changes to accounting rules or regulations, such as changes to revenue recognition or lease accounting guidance or a requirement to convert to international financial reporting standards, could adversely affect our operating results through increased cost of compliance.

**Risks Related to the Ownership of Our Common Stock**

***Our stock price may be volatile, which could result in a significant loss or impairment of your investment.***

On May 2, 2017, we completed our initial public offering (the “IPO”). Since the IPO, the price of our common stock as reported by The New York Stock Exchange (“NYSE”) has ranged from a low closing sales price of \$24.00 on December 24, 2018 to a high closing sales price of \$57.50 on April 5, 2018. In addition, the trading price of our common stock has been, and may continue to be, subject to wide price fluctuations in response to various factors, many of which are beyond our control, including those described above in “—Risks Related to our Business” and the following:

- actual or anticipated fluctuations in our quarterly or annual financial results;

- the financial guidance we may provide to the public, any changes in such guidance or our failure to meet such guidance;
- failure of industry or securities analysts to maintain coverage of us, changes in financial estimates by any industry or securities analysts that follow us or our failure to meet such estimates;
- downgrades in our credit ratings or the credit ratings of our competitors;
- market factors, including rumors, whether or not correct, involving us or our competitors;
- unfavorable market reactions to allegations regarding the safety of products sold by us or our competitors that are similar to products that we sell and costs or negative publicity arising out of any potential litigation and/or government investigations resulting therefrom;
- fluctuations in stock market prices and trading volumes of securities of similar companies;
- sales or anticipated sales of large blocks of our stock;
- short selling of our common stock by investors;
- limited “public float” in the hands of a small number of persons whose sales or lack of sales of our common stock could result in positive or negative pricing pressure on the market price for our common stock;
- additions or departures of key personnel;
- announcements of new store openings, commercial relationships, acquisitions or entry into new markets by us or our competitors;
- failure of any of our initiatives, including our growth strategy, to achieve commercial success;
- regulatory or political developments;
- changes in accounting principles or methodologies;
- litigation or governmental investigations;
- negative publicity about us in the media and online; and
- general financial market conditions or events.

Furthermore, the stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies, including ours. These fluctuations sometimes have been unrelated or disproportionate to the operating performance of those companies. These and other factors may cause the market price and demand for our common stock to fluctuate substantially, which may limit or prevent investors from readily selling their shares of common stock and may otherwise adversely affect the price or liquidity of our common stock.

In addition, in the past, when the market price of a stock has been volatile, holders of that stock have sometimes instituted securities class action litigation against the company that issued the stock. If any of our stockholders were to bring a lawsuit against us, we could incur substantial costs defending it or paying for settlements or damages. Such a lawsuit could also divert the time and attention of our management from our operating business. As a result, such litigation may adversely affect our business, financial condition and operating results.

***If securities or industry analysts do not publish or cease publishing research or reports about us, our business, our market, or our competitors, or if they change their recommendations regarding our common stock in a negative way, the price and trading volume of our common stock could decline.***

The trading market for our common stock is influenced by the research and reports that industry or securities analysts publish about us, our business, our market, or our competitors. If any of the analysts who cover us change their recommendation regarding our common stock in a negative way, or provide more favorable relative recommendations about our competitors, the price of our common stock would likely decline. If any analyst who covers us were to cease coverage of us or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our common stock price or trading volume to decline.

***The large number of shares eligible for public sale in the future, or the perception of the public that these sales may occur, could depress the market price of our common stock.***

The market price of our common stock could decline as a result of (i) sales of a large number of shares of our common stock in the market, particularly sales by our directors, employees (including our executive officers) and certain other significant stockholders, and (ii) a large number of shares of our common stock being registered or offered for sale. These sales, or the perception that these sales could occur, may depress the market price of our common stock. As of February 20, 2019, there were 97,727,273 shares of common stock outstanding, all of which were freely tradeable on the NYSE, except that any shares held by our affiliates, as that term is defined in Rule 144 under the Securities Act (“Rule 144”), may only be sold in compliance with the registration requirements of the Securities Act or under an exemption under Rule 144 or otherwise.

Additionally, as of February 20, 2019, approximately 9,772,026 shares of our common stock are issuable upon exercise of stock options that vest and are exercisable at various dates through November 6, 2028, with an average weighted exercise price of \$10.16 per share, and we have issued 10,165 shares of restricted stock with restrictions that lapse at various dates through November 2, 2020. Of such options, 6,395,267 are currently exercisable. We have filed a registration statement on Form S-8 under the Securities Act to register shares of our common stock issued or reserved for issuance under our stock incentive plans. The Form S-8 registration statement became effective immediately upon filing, and shares covered by that registration statement are eligible for sale in the public markets, subject to vesting restrictions and the limitations of Rule 144 applicable to affiliates.

All of our shares of common stock will be eligible for future sale, subject to the applicable volume, manner of sale, holding period and other limitations of Rule 144. In addition, our Sponsors have certain demand registration rights, and certain of our pre IPO stockholders have “piggy back” registration rights with respect to the common stock, subject to certain conditions and exceptions contained in a registration rights agreement.

***In the future, we expect to issue stock options, restricted stock and/or other forms of stock-based compensation, which have the potential to dilute stockholders’ value and cause the price of our common stock to decline.***

In the future, we expect to offer stock options, restricted stock and/or other forms of stock based compensation to our eligible employees, consultants and directors who are not executives or consultants of the Company or employees of Ares (as defined below) or Freeman Spogli (as defined below) or their respective affiliates. If we grant more equity awards to attract and retain key personnel, the expenses associated with such additional equity awards could materially adversely affect our results of operations and may also result in additional dilution to our stockholders. If any options that we issue are exercised or any restrictions on restricted stock that we issue lapse and those shares are sold into the public market, the market price of our common stock may decline. In addition, the availability of shares of common stock for award under our stock incentive plans or the grant of stock options, restricted stock or other forms of stock based compensation may adversely affect the market price of our common stock.

***Our ability to raise capital in the future may be limited.***

Our business and operations may consume resources faster than we anticipate. In the future, we may need to raise additional funds through the issuance of new equity securities, debt or a combination of both. Additional financing may not be available on favorable terms or at all. If adequate funds are not available on acceptable terms, we may be unable to fund our capital requirements. If we issue new debt securities, the debt holders would have rights senior to holders of our common stock to make claims on our assets and the terms of any debt could restrict our operations, including our ability to pay dividends on our common stock. If we issue additional equity securities or securities convertible into equity securities, existing stockholders will experience dilution and the new

equity securities could have rights senior to those of our common stock. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, you bear the risk of our future securities offerings reducing the market price of our common stock and diluting their interest.

***Our principal stockholders have substantial control over us, are able to influence corporate matters and may take actions that conflict with your interests and have the effect of delaying or preventing changes of control or changes in management, or limiting the ability of other stockholders to approve transactions they deem to be in their best interest.***

Our directors, executive officers and holders of more than 5% of our Class A common stock, together with their affiliates, beneficially own, in the aggregate, approximately 66.8% of our outstanding Class A common stock. Ares Corporate Opportunities Fund III, L.P. (“Ares”), a fund affiliated with Ares Management Corporation (“Ares Management”), beneficially owns, in the aggregate, approximately 26.7% of our outstanding Class A common stock, and FS Equity Partners VI, L.P. and FS Affiliates VI, L.P., funds affiliated with Freeman Spogli Management Co., L.P. (collectively “Freeman Spogli” or “Freeman Spogli & Co.” and together with Ares, our “Sponsors”) beneficially own, in the aggregate, approximately 12.9% of our outstanding Class A common stock. Additionally, Sands Capital Management, LLC beneficially owns approximately 9.1% of our outstanding Class A common stock, Joho Capital LLC beneficially owns approximately 5.8%, and Wellington Management Group LLP beneficially owns approximately 5.2%. As a result, these stockholders acting together, or Ares or Freeman Spogli acting alone, are able to exercise significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, such as a merger or other sale of us or our assets. The investor rights agreement by and among us, Ares and Freeman Spogli also contains agreements among our Sponsors with respect to voting on the election of our directors and committee memberships on our board of directors (the “Board”). The interests of Ares or Freeman Spogli could conflict in material respects with yours, and this concentration of ownership could limit your ability to influence corporate matters and may have the effect of delaying or preventing a third-party from acquiring control over us. Certain of the members of our Board also have relationships with our Sponsors. David B. Kaplan and Rachel H. Lee serve as officers and principals of certain Ares affiliated entities. In addition, NAX 18, LLC, a consulting entity controlled by Norman H. Axelrod, provides consulting services to certain Ares affiliated entities. Brad J. Brutocao and John M. Roth serve as officers and principals of certain Freeman Spogli affiliated entities. In addition, Peter Starrett Associates, a consulting entity controlled by Peter M. Starrett, provides consulting services to certain Freeman Spogli affiliated entities. Our certificate of incorporation provides that no officer or director of ours who is also an officer, director, employee, managing director or other affiliate of our Sponsors will be liable to us or our stockholders for breach of any fiduciary duty by reason of the fact that any such individual directs a corporate opportunity to our Sponsors instead of us, or does not communicate information regarding a corporate opportunity to us that the officer, director, employee, managing director or other affiliate has directed to our Sponsors.

***We do not currently expect to pay any cash dividends.***

The continued operation and growth of our business will require substantial funding. Accordingly, we do not currently expect to pay any cash dividends on shares of our common stock. Any determination to pay dividends in the future will be at the discretion of our Board and will depend upon our operating results, financial condition, contractual restrictions, restrictions imposed by applicable law and other factors our Board deem relevant. Additionally, under our Credit Facilities, our subsidiaries are currently restricted from paying cash dividends except in limited circumstances, and we expect these restrictions to continue in the future. Accordingly, realization of a gain on your investment in our common stock will depend on the appreciation of the price of our common stock, which may never occur. Investors seeking cash dividends in the foreseeable future should not purchase our common stock. See Item 5, “Market for Registrant’s Common Equity- Related Stockholder Matters and Issuer Purchases of Equity” for more information.

***As a result of our 2017 IPO, our costs have increased significantly, and our management is required to devote substantial time to complying with public company regulations, which will negatively impact our financial performance and could cause our results of operations or financial condition to suffer.***

In April 2017, we priced our IPO. As a result, we will continue to incur additional legal, accounting, insurance and other expenses that we did not incur as a private company, including costs associated with public company reporting requirements. We also have incurred and will incur costs associated with the Sarbanes-Oxley Act, Dodd-Frank Wall Street Reform and Consumer Protection Act and related rules implemented by the SEC. The expenses incurred by public companies generally for reporting and corporate governance purposes have been increasing. These rules and regulations increase our legal and financial compliance costs and make

some activities more time-consuming and costly, although we are currently unable to estimate these costs with any degree of certainty. In estimating these costs, we took into account expenses related to insurance, legal, accounting, and compliance activities, as well as other expenses. These laws and regulations can also make it more difficult or costly for us to obtain certain types of insurance, including director and officer liability insurance, and we may be forced to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage. These laws and regulations can also make it more difficult for us to attract and retain qualified persons to serve on our Board, our Board committees or as our executive officers. Furthermore, if we are unable to satisfy our obligations as a public company, we could be subject to delisting of our Class A common stock, fines, sanctions and other regulatory action and potentially civil litigation.

***Failure to establish and maintain effective internal controls in accordance with Sections 302 and 404 of the Sarbanes-Oxley Act could have an adverse effect on our business and stock price.***

We are required to comply with the SEC's rules implementing Sections 302 and 404 of the Sarbanes-Oxley Act, which require management to certify financial and other information in our quarterly and annual reports and provide an annual management report on the effectiveness of controls over financial reporting.

To comply with the requirements of Sections 302 and 404, we may need to undertake various actions, such as implementing new internal controls and procedures and hiring additional accounting or internal audit staff. Testing and maintaining internal controls can divert our management's attention from other matters that are important to the operation of our business. In addition, when evaluating our internal controls over financial reporting, we may identify material weaknesses that we may not be able to remediate in time to meet the applicable deadline imposed upon us for compliance with the requirements of Sections 302 and 404. If we identify material weaknesses in our internal controls over financial reporting or are unable to comply with the requirements of Sections 302 and 404 in a timely manner or assert that our internal controls over financial reporting are effective, or if our independent registered public accounting firm is unable to express an opinion as to the effectiveness of our internal controls over financial reporting, investors may lose confidence in the accuracy and completeness of our financial reports and the market price of our common stock could be negatively affected, and we could become subject to investigations by the NYSE, the SEC or other regulatory authorities, which could require additional financial and management resources.

***Anti-takeover provisions could impair a takeover attempt and adversely affect existing stockholders and the market value of our common stock.***

Certain provisions of our certificate of incorporation and bylaws and applicable provisions of Delaware law may have the effect of rendering more difficult, delaying or preventing an acquisition of the Company, even when this would be in the best interest of our stockholders. These provisions include:

- a classified Board;
- the sole power of a majority of our Board to fix the number of directors;
- the requirement that certain advance notice procedures be followed for our stockholders to submit nominations of candidates for election to our Board and to bring other proposals before a meeting of the stockholders;
- the power of our Board to amend our bylaws without stockholder approval;
- limitations on the removal of directors nominated by our Sponsors;
- the sole power of the Board, or our Sponsors in the case of a vacancy of one of their respective Board nominees, to fill any vacancy on the Board, whether such vacancy occurs as a result of an increase in the number of directors or otherwise;
- the ability of a majority of our Board (even if less than a quorum) to designate one or more series of preferred stock and issue shares of preferred stock without stockholder approval;

- the inability of stockholders to act by written consent if our Sponsors collectively own less than a majority of our outstanding Class A common stock;
- a requirement that, to the fullest extent permitted by law, certain proceedings against or involving us or our directors, officers or employees be brought exclusively in the Court of Chancery in the State of Delaware;
- the lack of cumulative voting rights for the holders of our Class A common stock with respect to the election of directors; and
- the inability of stockholders to call special meetings if our Sponsors collectively own less than a majority of our outstanding Class A common stock.

Further, Delaware law imposes conditions on the voting of “control shares” and on certain business combination transactions with “interested stockholders.”

Our issuance of shares of preferred stock could delay or prevent a change of control of the Company. Our Board has the authority to cause us to issue, without any further vote or action by our stockholders, shares of preferred stock, par value \$0.001 per share, in one or more series, to designate the number of shares constituting any series and to fix the rights, preferences, privileges and restrictions thereof, including dividend rights, voting rights, rights and terms of redemption, redemption price or prices and liquidation preferences of such series. The issuance of shares of preferred stock may have the effect of delaying, deferring or preventing a change in control of our Company without further action by our stockholders, even where stockholders are offered a premium for their shares.

In addition, the issuance of shares of preferred stock with voting rights may adversely affect the voting power of the holders of our other classes of voting stock either by diluting the voting power of our other classes of voting stock if they vote together as a single class, or by giving the holders of any such preferred stock the right to block an action on which they have a separate class vote even if the action were approved by the holders of our other classes of voting stock.

These provisions could delay or prevent hostile takeovers and changes in control or changes in our management. Also, the issuance of shares of preferred stock with dividend or conversion rights, liquidation preferences or other economic terms favorable to the holders of preferred stock could adversely affect the market price for our common stock by making an investment in our common stock less attractive. For example, a conversion feature could cause the trading price of our common stock to decline to the conversion price of the preferred stock. Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control or otherwise makes an investment in our common stock less attractive could limit the opportunity for our stockholders to receive a premium for their shares of our common stock and could also affect the price that some investors are willing to pay for our common stock.

**ITEM 1B. UNRESOLVED STAFF COMMENTS.**

None.

**ITEM 2. PROPERTIES .**

We have 100 U.S. warehouse-format stores located in 28 states, as shown in the chart below:

<b>State</b>	<b>Number of Stores</b>
Alabama	1
Arizona	5
California	10
Colorado	3
Florida	18
Georgia	7
Illinois	6
Indiana	1
Kansas	1
Kentucky	1
Louisiana	1
Maryland	1
Massachusetts	1
Missouri	1
Nevada	3
New Jersey	3
New Mexico	1
New York	1
North Carolina	2
Ohio	2
Oklahoma	1
Pennsylvania	2
Tennessee	3
Texas	15
Utah	2
Virginia	5
Washington	2
Wisconsin	1
<b>Total</b>	<b>100</b>

We opened 17 new stores during fiscal 2018. In addition to our warehouse-format stores, we operate one separate small 5,500 square foot design center located in New Orleans, Louisiana. Our headquarters, which we refer to as our store support center, is approximately 106,600 square feet and is located in Smyrna, Georgia. Additionally, we operate an approximately 37,000 square foot product review center in Smyrna, Georgia, as well as a 20,400 square foot sample fulfillment center in Marietta, GA.

Due to space constraints at our store support center, in October 2018, we signed a lease to relocate the store support center to a new facility in Atlanta, Georgia. The new location has approximately 185,473 square feet of office space with room for expansion. The lease has a twelve year term with rent expense of approximately \$469 thousand per month and is expected to commence in July 2019. We are still evaluating our options related to our current store support center. If we decide to exit the current lease, we could incur lease exit costs of up to \$9 million.

We lease our store support center, all of our stores and our distribution centers. Our leases generally have a term of ten to fifteen years, and generally have at least two renewal options for five years. Most of our leases provide for a minimum rent and typically include escalating rent increases. Our leases also generally require us to pay insurance, utilities, real estate taxes and repair and maintenance expenses.



**ITEM 3. LEGAL PROCEEDINGS .**

We are engaged in various legal actions, claims and proceedings arising in the ordinary course of business, including claims related to breach of contracts, product liabilities, intellectual property matters and employment related matters resulting from our business activities. As with most actions such as these, an estimation of any possible and/or ultimate liability cannot always be determined. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

**ITEM 4. MINE SAFETY DISCLOSURES .**

Not applicable.

**PART II**

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

**Market Information**

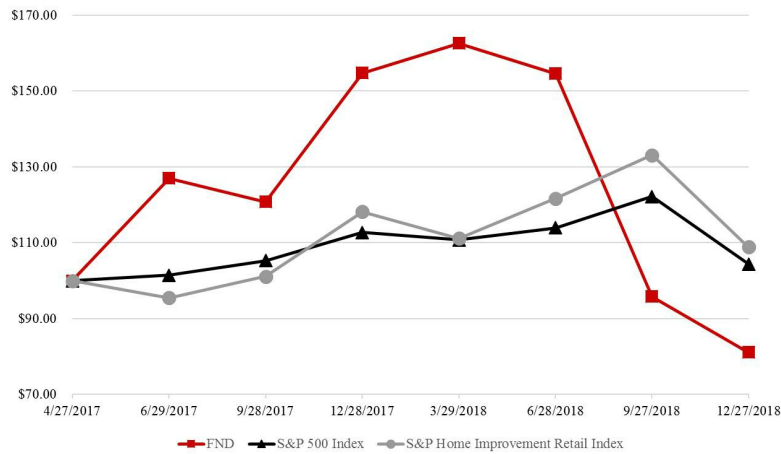
Our common stock has been listed on the NYSE under the symbol “FND” since our IPO on April 27, 2017. Prior to that date, there was no public market for our common stock. On February 20, 2019, there were 35 stockholders of record of our Class A common stock. The actual number of stockholders is greater than the number of record holders stated above, and includes stockholders who are beneficial owners, but whose shares are held in “street name” by brokers and other nominees. This number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

**Dividend Policy**

No dividends have been declared or paid on our common stock. We intend to continue to retain all available funds and any future earnings for use in the operation and growth of our business, and therefore we do not currently expect to pay any cash dividends on our common stock. Any future determination to pay dividends will be at the discretion of our Board and will depend on then existing conditions, including our operating results, financial condition, contractual restrictions, capital requirements, business prospects and other factors that our Board may deem relevant.

**Stock Performance Graph**

The following graph shows a comparison of cumulative total return to holders of common stock against the cumulative total return of the S&P 500 Index and the S&P 500 Home Improvement Retail Index from April 27, 2017 (the date our common stock commenced trading on the NYSE) through December 27, 2018. The comparison of the cumulative total returns for each investment assumes that \$100 was invested in our Class A common stock and the respective indices on April 27, 2017 through December 27, 2018, including reinvestment of any dividends. Historical share price performance should not be relied upon as an indication of future share price performance.



	<u>4/27/2017</u>	<u>6/29/2017</u>	<u>9/28/2017</u>	<u>12/28/2017</u>	<u>3/29/2018</u>	<u>6/28/2018</u>	<u>9/27/2018</u>	<u>12/27/2018</u>
FND	\$ 100.00	\$ 126.99	\$ 120.81	\$ 154.73	\$ 162.62	\$ 154.60	\$ 95.85	\$ 81.15
S&P 500 Index	\$ 100.00	\$ 101.49	\$ 105.28	\$ 112.72	\$ 110.77	\$ 113.93	\$ 122.22	\$ 104.39
S&P 500 Home Improvement Retail	\$ 100.00	\$ 95.46	\$ 101.10	\$ 118.17	\$ 111.16	\$ 121.71	\$ 133.16	\$ 108.86

**Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Repurchases of our Common Stock**

None.

**ITEM 6. SELECTED FINANCIAL DATA .**

The following table sets forth certain selected historical financial and operating data of the Company as of the dates and for the periods indicated. The following selected financial data are qualified by reference to, and should be read in conjunction with, the consolidated financial statements, related notes and other financial information, as well as in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations”. We operate on a 52- or 53-week fiscal year ending on the Thursday on or preceding December 31. The data presented contains references to fiscal 2014, fiscal 2015, fiscal 2016, fiscal 2017, and fiscal 2018, which represent our fiscal years ended December 25, 2014, December 29, 2016, December 28, 2017 and December 27, 2018 all of which were 52-week periods, and December 31, 2015, which was a 53-week period.

(in thousands, except per share amounts)(1)	Fiscal Year Ended				
	12/27/2018	12/28/2017	12/29/2016	12/31/2015(2)	12/25/2014
Net sales	\$ 1,709,848	\$ 1,384,767	\$ 1,050,759	\$ 784,012	\$ 584,588
Cost of sales	1,007,580	812,203	621,497	471,390	355,051
Gross profit	702,268	572,564	429,262	312,622	229,537
Operating expenses:					
Selling & store operating expenses	439,495	353,647	271,876	202,637	146,485
General & administrative expenses	105,327	84,661	64,025	49,917	38,984
Pre-opening expenses	26,145	16,485	13,732	7,380	7,412
Litigation settlement	—	—	10,500	—	—
Executive severance(3)	—	—	—	296	2,975
Total operating expenses	570,967	454,793	360,133	260,230	195,856
Operating income	131,301	117,771	69,129	52,392	33,681
Interest expense	8,917	13,777	12,803	9,386	8,949
Loss on early extinguishment of debt	—	5,442	1,813	—	—
Income before income taxes	122,384	98,552	54,513	43,006	24,732
Provision for income taxes	6,197	(4,236)	11,474	16,199	9,634
Net income	\$ 116,187	\$ 102,788	\$ 43,039	\$ 26,807	\$ 15,098
Earnings per share:					
Basic	\$ 1.20	\$ 1.13	\$ 0.52	\$ 0.32	\$ 0.18
Diluted	\$ 1.11	\$ 1.03	\$ 0.49	\$ 0.31	\$ 0.18
Weighted average shares outstanding:					
Basic	96,770	90,951	83,432	83,365	83,222
Diluted	104,561	99,660	88,431	86,281	85,652

(in thousands)	As of				
	12/27/2018	12/28/2017	12/29/2016	12/31/2015	12/25/2014
<b>Consolidated balance sheet data:</b>					
Cash and cash equivalents	\$ 644	\$ 556	\$ 451	\$ 318	\$ 279
Net working capital	158,029	146,856	95,550	109,565	78,577
Total assets	1,234,091	1,067,992	831,166	748,888	635,498
Total debt(4)	145,334	189,062	390,743	177,590	152,420
Total stockholders’ equity	584,309	442,860	134,283	312,365	282,236

(in thousands, except per share amounts)(1)	Fiscal Year Ended				
	12/27/2018	12/28/2017	12/29/2016	12/31/2015(2)	12/25/2014
<b>Consolidated statement of cash flows data:</b>					
Net cash provided by operating activities	\$ 185,624	\$ 109,207	\$ 89,456	\$ 20,380	\$ 43,594
Net cash used in investing activities	(151,397)	(102,253)	(74,648)	(45,021)	(39,069)
Net cash (used in) provided by financing activities	(34,139)	(6,849)	(14,675)	24,680	(4,421)
Cash dividends declared per share	—	—	2.43	—	—

Other financial data:	Fiscal Year Ended				
	12/27/2018	12/28/2017	12/29/2016	12/31/2015(2)	12/25/2014
Comparable store sales growth	9.2 %	16.6 %	19.4 %	13.5 %	15.8 %
Number of stores open at the end of the period(5)	101	84	70	58	48
Adjusted EBITDA (in thousands)(6)	\$ 191,939	\$ 158,781	\$ 108,398	\$ 72,868	\$ 51,208
Adjusted EBITDA margin	11.2 %	11.5 %	10.3 %	9.3 %	8.8 %

- (1) All of the earnings per share data, share numbers, share prices, and exercise prices have been adjusted on a retroactive basis to reflect the 321.820-for-one stock split effected on April 24, 2017.
- (2) The 53<sup>rd</sup> week in fiscal 2015 represented \$11.9 million in net sales, an estimated \$2.1 million in operating income and an estimated \$2.2 million in adjusted EBITDA. When presenting comparable store sales for fiscal 2015 and fiscal 2016, we have excluded the last week of fiscal 2015.
- (3) Represents costs incurred in connection with separation agreements with former officers.
- (4) Total debt consists of the current and long-term portions of our Credit Facilities, as well as debt discount and debt issuance costs.
- (5) Represents the number of our warehouse-format stores and our one small-format standalone design center.
- (6) EBITDA and Adjusted EBITDA (which are shown in the reconciliations below) have been presented in this filing as supplemental measures of financial performance that are not required by, or presented in accordance with, GAAP. We define EBITDA as net income before interest, loss on early extinguishment of debt, taxes, depreciation and amortization. We define Adjusted EBITDA as net income before interest, loss on early extinguishment of debt, taxes, depreciation and amortization, adjusted to eliminate the impact of certain items that we do not consider indicative of our core operating performance. Reconciliations of these measures to the equivalent measures under GAAP are set forth in the table below.

EBITDA and Adjusted EBITDA are key metrics used by management and our Board to assess our financial performance and enterprise value. We believe that EBITDA and Adjusted EBITDA are useful measures, as they eliminate certain expenses that are not indicative of our core operating performance and facilitate a comparison of our core operating performance on a consistent basis from period to period. We also use Adjusted EBITDA as a basis to determine covenant compliance with respect to our Credit Facilities, to supplement GAAP measures of performance to evaluate the effectiveness of our business strategies, to make budgeting decisions, and to compare our performance against that of other peer companies using similar measures. EBITDA and Adjusted EBITDA are also used by analysts, investors and other interested parties as performance measures to evaluate companies in our industry.

EBITDA and Adjusted EBITDA are non-GAAP measures of our financial performance and should not be considered as alternatives to net income as a measure of financial performance or any other performance measure derived in accordance with GAAP and they should not be construed as an inference that our future results will be unaffected by unusual or non-recurring items. Additionally, EBITDA and Adjusted EBITDA are not intended to be measures of liquidity or free cash flow for management's discretionary use. In addition, these non-GAAP measures exclude certain non-recurring and other charges. Each of these non-GAAP measures has its limitations as an analytical tool, and you should not consider them in isolation or as a substitute for analysis of our results as reported under GAAP. In evaluating EBITDA and Adjusted EBITDA, you should be aware that in the future we will incur expenses that are the same as or similar to some of the items eliminated in the adjustments made to determine EBITDA and Adjusted EBITDA, such as stock compensation expense, loss on asset disposal, executive recruiting/relocation, and other adjustments. Our presentation of EBITDA and Adjusted EBITDA should not be construed to imply that our future results will be unaffected by any such adjustments. Definitions and calculations of

EBITDA and Adjusted EBITDA differ among companies in the retail industry, and therefore EBITDA and Adjusted EBITDA disclosed by us may not be comparable to the metrics disclosed by other companies.

The reconciliations of net income to EBITDA and Adjusted EBITDA for the periods noted below are set forth in the table as follows:

(in thousands)	Fiscal Year Ended				
	12/27/2018	12/28/2017	12/29/2016	12/31/2015(2)	12/25/2014
Net income	\$ 116,187	\$ 102,788	\$ 43,039	\$ 26,807	\$ 15,098
Depreciation and amortization(a)	46,346	33,546	25,089	16,794	11,073
Interest expense	8,917	13,777	12,803	9,386	8,949
Loss on early extinguishment of debt(b)	—	5,442	1,813	—	—
Income tax expense (benefit)	6,197	(4,236)	11,474	16,199	9,634
EBITDA	177,647	151,317	94,218	69,186	44,754
Stock compensation expense(c)	6,514	4,959	3,229	3,258	2,323
Loss on asset disposal(d)	23	128	451	128	148
Executive severance(e)	—	—	—	296	2,975
Litigation settlement(f)	—	—	10,500	—	—
Other(g)	7,755	2,377	—	—	1,008
Adjusted EBITDA	\$ 191,939	\$ 158,781	\$ 108,398	\$ 72,868	\$ 51,208

- (a) Net of amortization of tenant improvement allowances and excludes deferred financing amortization, which is included as a part of interest expense in the table above.
- (b) Loss recorded as a result of non-cash write-off of certain deferred financing fees related to the refinancing of term and revolver borrowings in fiscal 2016. For fiscal 2017, the loss related to repaying a portion of our Term Loan Facility with our net proceeds from the IPO.
- (c) Non-cash charges related to stock-based compensation programs, which vary from period to period depending on timing of awards and forfeitures.
- (d) For fiscal 2014, fiscal 2015, fiscal 2016, fiscal 2017, and fiscal 2018, the losses related primarily to assets retired in connection with significant store remodels.
- (e) Represents one-time costs incurred in connection with separation agreements with former officers.
- (f) Legal settlement related to classwide settlement to resolve a lawsuit.
- (g) Other adjustments include amounts management does not consider indicative of our core operating performance. Amounts for fiscal 2018 primarily relate to costs associated with two secondary public offerings of our Class A common stock by certain of our stockholders, the closing of our distribution center near Miami, Florida, and losses from hurricanes Harvey and Florence. Amounts for fiscal 2017 relate to costs in connection with the IPO, two secondary public offerings of our Class A common stock by certain of our stockholders and expenses and losses, net of recoveries, from hurricanes Harvey and Irma. The Company did not sell any shares in any of the secondary offerings and did not receive any proceeds from the sales of shares by the selling stockholders. Amounts for fiscal 2014 relate to costs in connection with the IPO.

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

You should read the following discussion and analysis of our financial condition and results of operations together with “Selected Financial Data” and our consolidated financial statements and the related notes thereto and other financial information included elsewhere in this filing. This discussion and analysis contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those discussed in “Item 1A. Risk Factors.” See the cautionary note regarding forward-looking statements set forth at the beginning of Part I of this Annual Report.

**Overview**

Founded in 2000, Floor & Decor is a high-growth, differentiated, multi-channel specialty retailer of hard surface flooring and related accessories with 100 warehouse-format stores across 28 states as of December 27, 2018. We believe that we offer the industry’s broadest assortment of tile, wood, laminate, vinyl, and natural stone flooring along with decorative and installation accessories at everyday low prices. We appeal to a variety of customers, including our Pro, DIY and BIY customers. Our warehouse-format stores, which average approximately 75,000 square feet, carry on average approximately 3,800 flooring and decorative and installation accessory SKUs, 1.3 million square feet of flooring products and \$2.5 million of inventory at cost. We believe that our inspiring design centers and creative and informative visual merchandising also greatly enhance our customers’ renovation experience. In addition to our stores, our website *FloorandDecor.com* showcases our products.

We believe our strong financial results are a reflection of a growing domestic hard surface flooring market, a unique approach to selling hard surface flooring and our consistent and disciplined culture of innovation and reinvestment, together creating a differentiated business model in the hard surface flooring category. In fiscal 2018, we experienced our tenth year of comparable store sales growth, averaging 14.8% and for the past three years averaging 15.1%.

	Year Ended			CAGR
	12/27/2018	12/28/2017	12/29/2016	
Comparable stores sales	9.2 %	16.6 %	19.4 %	N/A
Number of warehouse-format stores	100	83	69	20.4 %
Net sales (in thousands)	\$ 1,709,848	\$ 1,384,767	\$ 1,050,759	27.6 %
Net income (in thousands)	\$ 116,187	\$ 102,788	\$ 43,039	64.3 %
Adjusted EBITDA (in thousands)	\$ 191,939	\$ 158,781	\$ 108,398	33.1 %

During fiscal 2018, we continued to make long-term key strategic investments, including:

- opening 17 new warehouse-format stores, including four new stores in densely populated markets in Boston, Seattle, Long Island and San Francisco Bay area, ending the year with 100 warehouse-format stores;
- focusing on innovative new products and localized assortments, supported by inspirational in-store and online visual merchandising solutions;
- augmenting the management team with new hires in store operations, store training, Pro and Commercial sales, e-commerce, supply chain, merchandising, real estate, information technology and inventory management;
- investing in our connected customer, in-store designer, and Pro customer personnel and technology;
- increasing proprietary credit offerings;
- adding more resources dedicated to serving our Pro customers;
- investing capital to continue enhancing the in-store shopping experience for our customers; and

- increasing and expanding marketing campaigns to articulate our unique features and benefits in the hard surface flooring market.

## **Fiscal 2019 – A Look At The Upcoming Year**

We believe that our compelling business model, in addition to the projected growth of the large and highly fragmented hard surface flooring market, provides us with an opportunity to significantly expand our store base in the U.S. from 100 warehouse format stores as of December 27, 2018 to approximately 400 stores nationwide within the next 10-15 years based on our internal research with respect to housing density, demographic data, competitor concentration and other variables in both new and existing markets. In 2019, we plan to grow our store base by approximately 20%. In addition to opening new stores, our focus will be on executing our core strategies as well as continuing to make investments that we believe will support our long-term growth, as outlined in “Item 1. Business - Our Growth Strategy.” Our ability to open profitable new stores depends on many factors, including the successful selection of new markets and store locations, our ability to negotiate leases on acceptable terms and our ability to attract highly qualified managers and staff. For further information see “Risk Factors—Risks Related to Our Business.”

### ***Key Performance Indicators***

We consider a variety of performance and financial measures in assessing the performance of our business. The key measures we use to determine how our business is performing are comparable store sales, the number of new store openings, gross profit and gross margin, operating income and EBITDA and Adjusted EBITDA.

#### *Comparable Store Sales*

Our comparable store sales growth is a significant driver of our net sales, profitability, cash flow and overall business results. We believe that comparable store sales growth is generated by continued focus on providing a dynamic and expanding product assortment in addition to other merchandising initiatives, quality of customer service, enhancing sales and marketing strategies, improving visual merchandising and overall aesthetic appeal of our stores and our website, effectively serving our Pro customers, continued investment in store staff and infrastructure, growing our proprietary credit offering, and further integrating connected customer strategies and other key information technology enhancements.

Comparable store sales refer to period-over-period comparisons of our net sales among the comparable store base, which has historically been when customers obtained possession of their product. Starting in fiscal 2018, when the new revenue recognition standard was adopted, our comparable store sales refer to period-over-period comparisons of our net sales based on when the customer obtains control of their product, which is typically at the time of sale and may be slightly different than our historically reported net sales due to timing of when final delivery of the product has occurred. A store is included in the comparable store sales calculation on the first day of the thirteenth full fiscal month following a store’s opening, which is when we believe comparability has been achieved. Since our e-commerce sales are fulfilled by individual stores, they are included in comparable store sales only to the extent the fulfilling store meets the above mentioned store criteria. Changes in our comparable store sales between two periods are based on net sales for stores that were in operation during both of the two periods. Any change in square footage of an existing comparable store, including remodels and relocations, does not eliminate that store from inclusion in the calculation of comparable store sales. Stores that are closed temporarily and relocated within their primary trade areas are included in same store sales. Additionally, any stores that were closed during the current or prior fiscal year are excluded from the definition of comparable stores.

Our fiscal 2015 year, which ended December 31, 2015, included a 53rd week. When presenting comparable store sales for fiscal 2015, we have excluded the last week of fiscal 2015.

Definitions and calculations of comparable store sales differ among companies in the retail industry, and therefore comparable store metrics disclosed by us may not be comparable to the metrics disclosed by other companies.

Comparable store sales allow us to evaluate how our retail stores are performing by measuring the change in period-over-period net sales. Various factors affect comparable store sales, including:

- national and regional economic conditions;
- the retail sales environment and other retail trends;
- the home improvement spending environment;



- the hard surface flooring industry trends;
- the impact of competition;
- changes in our product mix;
- changes in staffing at our stores;
- cannibalization resulting from the opening of new stores in existing markets;
- changes in pricing;
- changes in advertising and other operating costs; and
- weather conditions.

*Number of New Stores*

The number and timing of new store openings, and the costs and fixed lease obligations associated therewith, have had, and are expected to continue to have, a significant impact on our results of operations. The number of new stores reflects the number of stores opened during a particular reporting period. Before we open new stores, we incur pre-opening expenses, which are defined below. While net sales at new stores are generally lower than net sales at our stores that have been open for more than one year, our new stores have historically been profitable in their first year. Generally, our newer stores have also averaged higher comparable store sales growth than our total store average.

*Gross Profit and Gross Margin*

Our gross profit is variable in nature and generally follows changes in net sales. Our gross profit and gross margin can also be impacted by changes in our prices, our merchandising assortment, shrink, damage, selling of discontinued products, the cost to transport our products from the manufacturer to our stores and our distribution center costs. With respect to our merchandising assortment, certain of our products tend to generate somewhat higher margins than other products within the same product categories or among different product categories. We have experienced modest inflation increases in certain of our product categories, but historically have been able to source from a different manufacturer or pass increases onto our consumers with modest impact on our gross margin. Our gross profit and gross margin, which reflect our net sales and our cost of sales and any changes to the components thereof, allow us to evaluate our profitability and overall business results.

Gross profit is calculated as net sales less cost of sales. Gross profit as a percentage of net sales is referred to as gross margin. Cost of sales consists of merchandise costs, as well as freight costs to transport inventory to our distribution centers and stores, and duty and other costs that are incurred to distribute the merchandise to our stores. Cost of sales also includes shrinkage, damage product disposals, distribution, warehousing costs, sourcing and compliance costs. We receive cash consideration from certain vendors related to vendor allowances and volume rebates, which is recorded as a reduction of costs of sales as the inventory is sold or as a reduction of the carrying value of inventory while the inventory is still on hand. Costs associated with arranging and paying for freight to deliver products to customers is included in cost of sales. The components of our cost of sales may not be comparable to the components of cost of sales, or similar measures, of other retailers. As a result, data in this filing regarding our gross profit and gross margin may not be comparable to similar data made available by other retailers.

*Operating Income, EBITDA, Adjusted EBITDA*

Operating income, EBITDA and Adjusted EBITDA are key metrics used by management and our Board to assess our financial performance and enterprise value. We believe that operating income, EBITDA and Adjusted EBITDA are useful measures, as they eliminate certain expenses that are not indicative of our core operating performance and facilitate a comparison of our core operating performance on a consistent basis from period to period. We also use Adjusted EBITDA as a basis to determine covenant compliance with respect to our Credit Facilities, to supplement GAAP measures of performance to evaluate the effectiveness of our business strategies, to make budgeting decisions and to compare our performance against that of other peer companies using similar measures. Operating income, EBITDA and Adjusted EBITDA are also frequently used by analysts, investors and other interested parties as performance measures to evaluate companies in our industry.

EBITDA and Adjusted EBITDA are supplemental measures of financial performance that are not required by, or presented in accordance with, GAAP. We define EBITDA as net income before interest, loss on early extinguishment of debt, taxes, depreciation and amortization. We define Adjusted EBITDA as net income before interest, loss on early extinguishment of debt, taxes, depreciation and amortization, adjusted to eliminate the impact of certain items that we do not consider indicative of our core operating performance.

EBITDA and Adjusted EBITDA are non-GAAP measures of our financial performance and should not be considered as alternatives to net income as a measure of financial performance or any other performance measure derived in accordance with GAAP and they should not be construed as an inference that our future results will be unaffected by unusual or non-recurring items. Additionally, EBITDA and Adjusted EBITDA are not intended to be measures of liquidity or free cash flow for management's discretionary use. In addition, these non-GAAP measures exclude certain non-recurring and other charges. Each of these non-GAAP measures has its limitations as an analytical tool, and you should not consider them in isolation or as a substitute for analysis of our results as reported under GAAP. In evaluating EBITDA and Adjusted EBITDA, you should be aware that in the future we will incur expenses that are the same as or similar to some of the items eliminated in the adjustments made to determine EBITDA and Adjusted EBITDA, such as stock compensation expense, loss (gain) on asset disposal, executive recruiting/relocation, and other adjustments. Our presentation of EBITDA and Adjusted EBITDA should not be construed to imply that our future results will be unaffected by any such adjustments. Definitions and calculations of EBITDA and Adjusted EBITDA differ among companies in the retail industry, and therefore EBITDA and Adjusted EBITDA disclosed by us may not be comparable to the metrics disclosed by other companies.

***Other Key Financial Definitions***

*Net Sales*

The retail sector in which we operate is cyclical, and consequently our sales are affected by general economic conditions. Purchases of our products are sensitive to trends in the levels of consumer spending, which are affected by a number of factors such as consumer disposable income, housing market conditions, unemployment trends, stock market performance, consumer debt levels and consumer credit availability, interest rates and inflation, tax rates and overall consumer confidence in the economy.

Net sales reflect our sales of merchandise, less discounts and estimated returns and include our in-store sales and e-commerce sales. In certain cases, we arrange and pay for freight to deliver products to customers and bill the customer for the estimated freight cost, which is also included in net sales. Revenue is recognized when we satisfy the performance obligations in contracts with our customers. Our performance obligations for our retail store sales, as well as for orders placed through our website and shipped to our customers, are satisfied at the point-of-sale, which is the point at which the customer obtains control of the inventory.

*Selling and Store Operating Expenses*

We expect that our selling and store operating expenses will increase in future periods with future growth. Selling and store operating expenses consist primarily of store personnel wages, bonuses and benefits, rent and infrastructure expenses, supplies, depreciation and amortization, training expenses and advertising costs. Credit card fees, insurance, personal property taxes and other miscellaneous operating costs are also included.

The components of our selling and store operating expenses may not be comparable to the components of similar measures of other retailers.

*General and Administrative Expenses*

We expect that our general and administrative expenses will increase in future periods with future growth and in part due to additional legal, accounting, insurance and other expenses that we expect to incur as a result of being a public company, including compliance with the Sarbanes-Oxley Act. General and administrative expenses include both fixed and variable components, and therefore, are not directly correlated with net sales.

General and administrative expenses consist primarily of costs incurred outside of our stores and include administrative personnel wages in our store support center and regional functions, bonuses and benefits, supplies, depreciation and amortization, and store support center expenses. Insurance, legal expenses, information technology costs, consulting and other miscellaneous operating costs are also included.

The components of our general and administrative expenses may not be comparable to the components of similar measures of other retailers.

*Pre-opening Expenses*

We account for non-capital operating expenditures incurred prior to opening a new store or relocating an existing store as “pre-opening” expenses in our consolidated statements of income. Our pre-opening expenses begin, on average, three to six months in advance of a store opening or relocating due to, among other things, the amount of time it takes to prepare a store for its grand opening. Pre-opening expenses primarily include the following: rent, advertising, training, staff recruiting, utilities, personnel, and equipment rental. A store is considered to be relocated if it is closed temporarily and re-opened within the same primary trade area.

**Results of Operations**

The following table summarizes key components of our results of operations for the periods indicated, in dollars and as a percentage of net sales:

(in thousands)	Year Ended				\$ Increase/(Decrease)	% Increase/(Decrease)
	12/27/2018		12/28/2017			
	Actual	% of Sales	Actual	% of Sales		
Net sales	\$ 1,709,848	100.0 %	\$ 1,384,767	100.0 %	\$ 325.1	23.5 %
Cost of sales	1,007,580	58.9	812,203	58.7	195.4	24.1
Gross profit	702,268	41.1	572,564	41.3	129.7	22.7
Operating expenses:						
Selling & store operating expenses	439,495	25.7	353,647	25.5	85.8	24.3
General & administrative expenses	105,327	6.2	84,661	6.1	20.7	24.4
Pre-opening expenses	26,145	1.5	16,485	1.2	9.7	58.6
Total operating expenses	570,967	33.4	454,793	32.8	116.2	25.5
Operating income	131,301	7.7	117,771	8.5	13.5	11.5
Interest expense	8,917	0.5	13,777	1.0	(4.9)	(35.3)
Loss on early extinguishment of debt	—	—	5,442	0.4	(5.4)	(100.0)
Income before income taxes	122,384	7.2	98,552	7.1	23.8	24.2
Provision for income taxes	6,197	0.4	(4,236)	(0.3)	10.4	NM
Net income	\$ 116,187	6.8 %	\$ 102,788	7.4 %	\$ 13.4	13.0 %

(in thousands)	Year Ended				\$ Increase/(Decrease)	% Increase/(Decrease)
	12/28/2017		12/29/2016			
	Actual	% of Sales	Actual	% of Sales		
Net sales	\$ 1,384,767	100.0 %	\$ 1,050,759	100.0 %	\$ 334.0	31.8 %
Cost of sales	812,203	58.7	621,497	59.1	190.7	30.7
Gross profit	572,564	41.3	429,262	40.9	143.3	33.4
Operating expenses:						
Selling & store operating expenses	353,647	25.5	271,876	25.9	81.8	30.1
General & administrative expenses	84,661	6.1	64,025	6.1	20.6	32.2
Pre-opening expenses	16,485	1.2	13,732	1.3	2.8	20.0
Litigation settlement	—	—	10,500	1.0	(10.5)	(100.0)
Total operating expenses	454,793	32.8	360,133	34.3	94.7	26.3
Operating income	117,771	8.5	69,129	6.6	48.6	70.4
Interest expense	13,777	1.0	12,803	1.2	1.0	7.6
Loss on early extinguishment of debt	5,442	0.4	1,813	0.2	3.6	200.2
Income before income taxes	98,552	7.1	54,513	5.2	44.0	80.8
Provision for income taxes	(4,236)	(0.3)	11,474	1.1	(15.7)	NM
Net income	\$ 102,788	7.4 %	\$ 43,039	4.1 %	\$ 59.7	138.8 %

NM- Not Meaningful

	Year Ended		
	12/27/2018	12/28/2017	12/29/2016
Comparable stores sales	9.2 %	16.6 %	19.4 %
Comparable average ticket	(0.6)%	1.7 %	3.6 %
Comparable customer transactions	10.0 %	14.8 %	14.7 %
Number of warehouse-format stores	100	83	69
Adjusted EBITDA (in thousands)	\$ 191,939	\$ 158,781	\$ 108,398
Adjusted EBITDA margin	11.2 %	11.5 %	10.3 %

**Net Sales**

Net sales during fiscal 2018 increased \$325.1 million, or 23.5%, compared to fiscal 2017 which does not reflect \$8.1 million of prior year sales recognized through the opening balance sheet adjustment described in “Item 8. Recent Accounting Pronouncements.” Four out of six of our product categories experienced comparable store sales increases during the period, driven by increases in laminate/luxury vinyl plank, installation materials and decorative accessories that were above our average for fiscal 2018. Our comparable store sales increased 9.2%, or \$128.2 million, while our non-comparable store sales contributed \$188.8 million. The increase in comparable store sales was largely driven by a 10.0% increase in comparable customer transactions, slightly offset by a 0.6% decrease in comparable average ticket growth. We believe the increase in net sales and customer transactions are due to the execution of our key strategic investments. As described in the “Overview” section above, we believe our enhanced Pro, designer, merchandising, connected customer, marketing and visual merchandising strategies, along with new innovative products led to our sales growth. Non-comparable store sales were driven by the opening of 17 new stores during fiscal 2018.

Net sales during fiscal 2017 increased \$334.0 million, or 31.8%, compared to fiscal 2016. All of our product categories experienced comparable store sales increases during the period, driven by increases in laminate/luxury vinyl plank and decorative accessories that were above our average for fiscal 2017. Our comparable store sales increased 16.6%, or \$173.1 million, while our non-comparable store sales contributed \$160.9 million. The increase in comparable store sales was largely driven by a 14.8% increase in comparable customer transactions and to a lesser extent a 1.7% increase in comparable average ticket growth. Comparable customer transactions and average ticket are measured at the time of sale, which may be slightly different than our reported sales due to timing of when final delivery of the product has occurred. We believe the increase in net sales, customer transactions and average ticket are due to the execution of our key strategic investments and an improved U.S. flooring market. As described in the “Overview” section above, we believe our enhanced Pro, merchandising, connected customer, marketing and visual merchandising strategies, along with new innovative products led to our sales growth. In addition, comparable stores sales benefited by approximately 200 basis points from the continued recovery in the areas impacted by Hurricane Harvey. Non-comparable store sales were driven by the opening of 14 new stores during fiscal 2017.

**Gross Profit and Gross Margin**

Gross profit for fiscal 2018 increased \$129.7 million, or 22.7%, compared to fiscal 2017. This increase in gross profit was primarily the result of increased sales slightly offset by lower product margins. Gross margin for fiscal 2018 decreased approximately 20 basis points to 41.1% from 41.3% in fiscal 2017. This decrease in gross margin was primarily attributable to higher transportation costs and lower landed margin partially offset by higher other vendor allowances.

Gross profit for fiscal 2017 increased \$143.3 million, or 33.4%, compared to fiscal 2016. This increase in gross profit was primarily the result of increased sales and to a lesser extent higher product margins. Gross margin for fiscal 2017 increased approximately 40 basis points to 41.3% from 40.9% in fiscal 2016. This increase in gross margin was primarily attributable to higher product margin of approximately 75 basis points and approximately 10 basis points due to lower inventory shrinkage and damage, partially offset by approximately 30 basis points of higher distribution center costs due to expanding approximately 2.4x to 2.9 million square feet.

**Selling and Store Operating Expenses**

Selling and store operating expenses in fiscal 2018 increased by \$85.8 million, or 24.3% from fiscal 2017, due primarily to the addition of 17 new stores in fiscal 2018. As a percentage of net sales, our selling and store operating expenses increased approximately 20 basis points to 25.7%. Comparable store selling and store operating expenses as a percentage of comparable store sales decreased by approximately 90 basis points, as we leveraged occupancy and personnel expenses on higher net sales.

Selling and store operating expenses in fiscal 2017 increased by \$81.8 million, or 30.1% from fiscal 2016, due primarily to the addition of 14 new stores in fiscal 2017, and to a lesser extent increased personnel and occupancy expenses at our mature stores to support a 16.6% same store sales increase. As a percentage of net sales, our selling and store operating expenses decreased approximately 40 basis points to 25.5%. Comparable store selling and store operating expenses as a percentage of comparable store sales decreased by approximately 140 basis points, as we leveraged occupancy and personnel expenses on higher net sales.

***General and Administrative Expenses***

General and administrative expenses, which are typically expenses incurred outside of our stores, increased \$20.7 million in fiscal 2018, or 24.4% from fiscal 2017 due to our continued investments in personnel for our regional and store support functions in support of our store growth, in addition to costs associated with the exiting of our distribution center near Miami, Florida and compliance with the Sarbanes-Oxley Act. Our general and administrative expenses as a percentage of net sales increased 10 basis points in fiscal 2018 to 6.2% compared to 6.1% in fiscal 2017.

General and administrative expenses, which are typically expenses incurred outside of our stores, increased \$20.6 million in fiscal 2017, or 32.2% from fiscal 2016, due to our continued investments in personnel for our regional and store support functions in support of our store growth and higher legal and consulting costs as a result of indirect costs associated with our IPO and 2017 secondary offerings. Our general and administrative expenses as a percentage of net sales remained flat year over year.

***Pre-Opening Expenses***

Pre-opening expenses in fiscal 2018 increased \$9.7 million, or 58.6% from fiscal 2017. The increase is primarily due to a greater number of new stores opened or planned to be opened for which pre-opening expenses were incurred, as well as higher average occupancy, labor and marketing costs due to targeted locations being in higher cost metropolitan locations during fiscal 2018 compared to fiscal 2017. During fiscal 2018, we opened 17 stores, as well as one relocation, and incurred costs for three additional stores and one relocation planned to open in 2019, as compared to opening 14 stores, and incurring costs for four additional stores as well as one relocation planned to open in 2018 during fiscal 2017.

Pre-opening expenses in fiscal 2017 increased \$2.8 million, or 20.0% from fiscal 2016. The increase is primarily due to a greater number of new stores opened or planned to be opened for which pre-opening expenses were incurred, as well as higher average occupancy costs due to targeted locations being in higher cost metropolitan locations during fiscal 2017 compared to fiscal 2016. During fiscal 2017, we opened 14 stores, as well as one relocation, and incurred costs for four additional stores planned to open in 2018, as compared to opening 12 stores, and incurring costs for three additional stores planned to open as well as one relocation in 2017 during fiscal 2016.

***Interest Expense***

Interest expense in fiscal 2018 decreased \$4.9 million, or 35.3% compared to fiscal 2017. The decrease in interest expense was primarily due to our average total debt decreasing to \$170.0 million in fiscal 2018 compared to \$261.5 million in fiscal 2017.

Interest expense in fiscal 2017 increased \$1.0 million, or 7.6% compared to fiscal 2016. The increase in interest expense was primarily due to our average total debt increasing to \$261.5 million in fiscal 2017 compared to \$225.4 million in fiscal 2016. The increase in average total debt was due to paying a special dividend of \$202.5 million, making related cash payments of \$22.5 million in respect of certain options to purchase our common stock and refinancing our debt in the fiscal fourth quarter of 2016, partially offset by paying down approximately \$192.0 million of our debt with our net IPO proceeds during the fiscal second quarter of 2017. The increase in interest expense was partially offset by a lower effective interest rate of 5.3% for fiscal 2017 from 5.7% for fiscal 2016.

***Taxes***

The provision for income taxes in fiscal 2018 increased \$10.4 million from fiscal 2017. The effective tax rate was 5.1% compared to (4.3)% for fiscal 2018 compared to fiscal 2017, respectively. The increase in the effective tax rate was primarily due to the tax benefit recognized in fiscal 2017 related to the remeasurement of our deferred tax assets and liabilities based on the new 21% corporate income tax rate enacted in December 2017.

The provision for income taxes in fiscal 2017 decreased \$15.7 million, or 136.9% from fiscal 2016. The effective tax rate was (4.3)% compared to 21.0% for fiscal 2017 compared to fiscal 2016, respectively. The decrease in the effective tax rate was primarily due to the combination of the excess tax benefit related to stock options exercised and the tax benefit related to adjusting our deferred tax rate to our anticipated future rate due to new tax reform legislation enacted in December 2017.

### **Seasonality**

Historically, our business has had very little seasonality. Our specialty hard surface flooring and decorative home product offering makes us less susceptible to holiday shopping seasonal patterns compared to other retailers. However, we generally conduct a clearance event during our third fiscal quarter followed by a smaller clearance event towards the end of the year. The timing of these clearance events is driven by operational considerations rather than customer demand and could change from year to year.

### **Liquidity and Capital Resources**

Liquidity is provided primarily by our cash flows from operations and our ABL Facility. During fiscal 2018, we generated \$185.6 million in cash from operating activities. As of December 27, 2018, we had \$289.8 million in unrestricted liquidity, consisting of \$0.6 million in cash and cash equivalents and \$289.2 million immediately available for borrowing under the ABL Facility without violating any covenants thereunder.

Our primary cash needs are for merchandise inventories, payroll, store rent, and other operating expenses and capital expenditures associated with opening new stores and remodeling existing stores, as well as information technology, e-commerce and store support center infrastructure. We also use cash for the payment of taxes and interest.

The most significant components of our operating assets and liabilities are merchandise inventories and accounts payable, and to a lesser extent accounts receivable, prepaid expenses and other assets, other current and non-current liabilities, taxes receivable and taxes payable. Our liquidity is not generally seasonal, and our uses of cash are primarily tied to when we open stores and make other capital expenditures. We believe that cash expected to be generated from operations and the availability of borrowings under the ABL Facility will be sufficient to meet liquidity requirements, anticipated capital expenditures and payments due under our Credit Facilities for at least the next 12 months.

Merchandise inventory is our most significant working capital asset and is considered “in-transit” or “available for sale”, based on whether we have physically received the products at an individual store location or in one of our three distribution centers. In-transit inventory generally varies due to contractual terms, country of origin, transit times, international holidays, weather patterns and other factors, but for the last two years, approximately 16% of our inventory was in-transit, while roughly 84% was available for sale in our stores or at one of our three distribution centers.

We measure realizability of our inventory by monitoring sales, gross margin, inventory aging, weeks of supply or inventory turns as well as by reviewing SKUs that have been determined by our merchandising team to be discontinued. Based on our analysis of these factors, we believe our inventory is realizable.

Twice a year, we conduct a clearance event with the goal of selling through discontinued inventory, followed by donations of the aged discontinued inventory that we are unable to sell. We generally conduct a larger clearance event during our third fiscal quarter followed by a smaller clearance event towards the end of the fiscal year. We define aged discontinued inventory as inventory in discontinued status for more than 12 months that we intend to donate. As of December 27, 2018 we had \$1.6 million of aged discontinued inventory.

Total capital expenditures in fiscal 2019 are planned to be between approximately \$220 million to \$230 million and will be funded primarily by cash generated from operations and borrowings under the ABL Facility. We intend to make the following capital expenditures in fiscal 2019:

- Open 20 stores and start construction on stores opening in early fiscal 2020 using approximately \$146 million to \$153 million of cash;
- Invest in existing store remodeling projects and our distribution centers using approximately \$39 million to \$41 million of cash; and

- Invest in information technology infrastructure, e-commerce and other store support center initiatives using approximately \$35 million to \$36 million of cash.

During the first quarter of fiscal 2018, we relocated all the existing inventory from our currently leased distribution center near Miami, Florida to the newly leased distribution center near Savannah, Georgia and incurred related costs of approximately \$0.5 million.

#### ***Cash Flow Analysis***

A summary of our operating, investing and financing activities are shown in the following table:

<b>(in thousands)</b>	<b>Fiscal Year Ended</b>		
	<b>12/27/2018</b>	<b>12/28/2017</b>	<b>12/29/2016</b>
Net cash provided by operating activities	\$ 185,624	\$ 109,207	\$ 89,456
Net cash used in investing activities	(151,397)	(102,253)	(74,648)
Net cash used in financing activities	(34,139)	(6,849)	(14,675)
Net increase in cash and cash equivalents	\$ 88	\$ 105	\$ 133

#### ***Net Cash Provided By Operating Activities***

Cash from operating activities consists primarily of net income adjusted for non-cash items, including depreciation and amortization, write-off of deferred issuance costs on extinguishment of debt, stock-based compensation, deferred taxes and the effects of changes in operating assets and liabilities.

Net cash provided by operating activities was \$185.6 million for fiscal 2018 and \$109.2 million for fiscal 2017. The change in net cash provided by operating activities was primarily the result of an increase in net income and working capital to support future sales and new store openings. The modest 10% growth in inventory in fiscal 2018 was due to opening 17 new stores and modest improvement in inventory turns in existing stores throughout fiscal 2018.

Net cash provided by operating activities was \$109.2 million for fiscal 2017 and \$89.5 million for fiscal 2016. The change in net cash provided by operating activities was primarily the result of an increase in net income and adjustments to net income driven by depreciation related to capital expenditures. This was slightly offset by increased working capital to support future sales and new store openings. At the end of fiscal 2017, we increased our inventory to prepare for our Savannah and Miami area distribution centers' relocations, and to improve our in-stock inventory in anticipation of factory closures for Chinese New Year.

#### ***Net Cash Used In Investing Activities***

Investing activities consist primarily of capital expenditures for new store openings, existing store remodels (including leasehold improvements, new racking, new fixtures, new vignettes and new design centers) and new infrastructure and information systems.

Capital expenditures were \$151.4 million compared to \$102.3 million for fiscal 2018 and fiscal 2017, respectively. The growth is primarily related to opening more new stores in fiscal 2018 as well as capital expenditures for stores opening in early fiscal 2019 compared to the same period in fiscal 2017. For fiscal 2018, approximately 65% of capital expenditures was for new stores, 20% was for existing store remodel and distribution center investments, and the remainder was for information technology and e-commerce investments.

Capital expenditures were \$102.3 million compared to \$74.6 million for fiscal 2017 and fiscal 2016, respectively. The growth is primarily related to opening more new stores in fiscal 2017 as well as capital expenditures for stores opening in early fiscal 2018 compared to the same period in fiscal 2016. For fiscal 2017, approximately 50% of capital expenditures was for new stores, 35% was for existing store remodel and distribution center investments, and the remainder was for information technology and e-commerce investments.



### ***Net Cash Used In Financing Activities***

Financing activities consist primarily of borrowings and related repayments under our credit agreements, as well as dividends paid to common stockholders.

Net cash used in financing activities was \$34.1 million for fiscal 2018 and \$6.8 million for fiscal 2017. The net cash used in financing activities for fiscal 2018 was driven by a net paydown on the ABL Facility of \$41.0 million, slightly offset by proceeds received from stock options exercised of \$10.5 million.

Net cash used in financing activities was \$6.8 million for fiscal 2017 and \$14.7 million for fiscal 2016. The net cash used in financing activities for fiscal 2017 was driven by a net paydown on the ABL Facility of \$9.0 million and proceeds received from stock options exercised of \$8.9 million. We also received aggregate net proceeds of approximately \$192.3 million in connection with the IPO, after deducting underwriting discounts and commissions and other offering expenses, and used the net proceeds of approximately \$192.0 million to repay a portion of the amounts outstanding under the Term Loan Facility. Additionally, we utilized \$2.0 million of cash from operations to repay a portion of the amounts outstanding under the Term Loan Facility.

### ***Our Credit Facilities***

We have two arrangements governing our material outstanding indebtedness: our ABL Facility and our Term Loan Facility.

The indebtedness outstanding under our Credit Facilities is secured by substantially all of our assets. In particular, the indebtedness outstanding under (i) the ABL Facility is secured by a first-priority security interest in all of our current assets, including inventory and accounts receivable, and a second-priority security interest in the collateral that secures the Term Loan Facility on a first-priority basis, and (ii) the Term Loan Facility is secured by a first-priority security interest in all of our fixed assets and intellectual property, and a second-priority interest in the collateral that secures the ABL Facility on a first-priority basis.

The Term Loan Facility requires quarterly repayments of approximately \$875 thousand, which commenced on December 31, 2016, with the remainder due and payable at maturity.

The Term Loan Facility has no financial maintenance covenants. As of December 27, 2018, we were in compliance in all material respects with the covenants of the Credit Facilities and no Event of Default (as defined in the credit agreements governing our Credit Facilities) had occurred.

As of December 27, 2018, the Term Loan Facility bore interest based on one of the following rates, at our option:

- i) Adjusted LIBOR Rate plus a margin of 2.50%
- ii) Base Rate plus a margin of 1.50%. Base Rate defined as the greater of the following:
  - (a) the base rate in effect on such day,
  - (b) the federal funds rate plus 0.50%,
  - (c) the adjusted LIBOR rate for the interest period of one month plus a margin of 1.00%.

On March 31, 2017, the Company entered into a repricing amendment to the Term Loan Facility. This amendment reduced the margins applicable to the term loan from 3.25% per annum (subject to a leverage-based step-down to 2.75%) to 2.50% per annum (subject to a leverage-based step-down to 2.00%) in the case of base rate loans, and from 4.25% per annum (subject to a leverage-based step-down to 3.75%) to 3.50% per annum (subject to a leverage-based step-down to 3.00%) in the case of LIBOR loans (subject to a 1.00% floor on LIBOR loans), provided that each of the leverage-based step-downs was contingent upon the consummation of the IPO.

In October 2017, we met the requirements to lower our interest rate on the Term Loan Facility by an additional 50 basis points (pursuant to the leverage-based step-down) to 4.00% for LIBOR loans, based on a margin of 3.00% and a 1.00% floor.

On November 22, 2017, we entered into an amendment to the Term Loan Facility. The aggregate principal amount of loans outstanding under the Term Loan Facility on the date of such amendment was approximately \$152.5 million. This November 2017 amendment reduced the margins applicable to the Term Loan Facility (x) in the case of base rate loans, from 2.00% per annum (due to operation of a leverage-based step-down from 2.50%) to 1.75% per annum (subject to a ratings based step-down to 1.50%), and (y) in the case of LIBOR loans, from 3.00% per annum (due to operation of a leverage-based step-down from 3.50%) to 2.75% per annum (subject to a ratings based step-down to 2.50%) (subject to a 1.00% floor on LIBOR loans). The amount and terms of the Term Loan Facility were otherwise unchanged.

The ABL Facility initially accrued interest ranging from LIBOR + 1.50% to LIBOR + 2.00%, and as of December 27, 2018 was subject to a pricing grid based on average daily availability under such facility ranging from LIBOR + 1.25% to 1.50%. The ABL Facility allows us to borrow up to \$300 million, subject to the borrowing base requirements, set forth in the credit agreement governing the ABL Facility.

On December 11, 2018, we exercised our right under the accordion feature of the ABL Facility to increase our total borrowing capacity under the ABL Facility by \$100.0 million, bringing the aggregate commitments thereunder to \$300.0 million (the “ABL Commitment Increase”). The ABL Commitment Increase was provided by Wells Fargo Bank, National Association, Bank of America, N.A. and Regions Bank, existing lenders party to the credit agreement governing the ABL Facility immediately prior to the ABL Commitment Increase. Borrowings under the ABL Commitment Increase continue to be subject to the terms and conditions set forth in the credit agreement governing the ABL Facility, and all other terms of the ABL Facility remain unchanged. As of December 27, 2018, we had the ability to access \$289.2 million of unused borrowings under the ABL Facility without violating any covenants thereunder and had \$10.9 million in outstanding letters of credit thereunder.

The credit agreements governing our Credit Facilities contain customary restrictive covenants that, among other things and with certain exceptions, limit our ability to (i) incur additional indebtedness and liens in connection therewith, (ii) pay dividends and make certain other restricted payments, (iii) effect mergers or consolidations, (iv) enter into transactions with affiliates, (v) sell or dispose of property or assets, and (vi) engage in unrelated lines of business. In addition, these credit agreements subject us to certain reporting obligations and require that we satisfy certain financial covenants, including, among other things, a requirement that if borrowings under the ABL Facility exceed 90% of availability, we will maintain a certain fixed charge coverage ratio (defined as consolidated EBITDA less non-financed capital expenditures and income taxes paid to consolidated fixed charges, in each case as more fully defined in the credit agreement governing the ABL Facility).

For more information on our Credit Facilities, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources.”

#### **U.S. Tariffs and Global Economy**

The current domestic and international political environment, including existing and potential changes to U.S. policies related to global trade and tariffs, have resulted in uncertainty surrounding the future state of the global economy. In September 2018, the U.S. imposed tariffs of 10% on many products from China, and the U.S. administration has announced an intention to increase that amount to 25% in March 2019 if a trade agreement cannot be reached. Approximately half of the products we sell are imported from China, the vast majority of which are impacted by these tariffs. While we are still analyzing the impact these tariffs may have on our business, we believe we can mitigate some of these cost increases through negotiating lower costs from our vendors, increasing retail pricing as we deem appropriate and potentially sourcing from alternative destinations. As part of these efforts, we expect the recently enacted tariffs to increase our inventory costs and associated cost of goods sold in the first quarter of 2019 as we incur the tariffs and import more products ahead of the potentially higher tariffs. We expect our efforts to mitigate a substantial portion of the overall effect of increased tariffs, including a material increase to our inventory costs in fiscal 2019. Potential costs and any attendant impact on pricing arising from these tariffs and any further expansion in the types or levels of tariffs implemented could require us to modify our current business practices and could adversely affect our business, financial condition and results of operations.

### Contractual Obligations

We enter into long-term obligations and commitments in the normal course of business, primarily debt obligations and non-cancelable operating leases. As of December 27, 2018, our contractual cash obligations over the next several periods were as follows:

(in thousands)	Payments due by period						
	Total	12/26/2019	12/31/2020	12/30/2021	12/29/2022	12/28/2023	Thereafter
Term loans	\$ 149,000	\$ 3,500	\$ 4,375	\$ 2,625	\$ 3,500	\$ 135,000	\$ —
Revolving loan	—	—	—	—	—	—	—
Estimated interest(1)	29,345	6,577	6,438	6,263	6,106	3,961	—
Operating leases(2)	1,308,717	114,076	131,394	123,249	116,925	112,430	710,643
Letters of credit	10,859	10,859	—	—	—	—	—
Purchase obligations(3)	179,703	178,367	1,012	324	—	—	—
<b>Total</b>	<b>\$ 1,677,624</b>	<b>\$ 313,379</b>	<b>\$ 143,219</b>	<b>\$ 132,461</b>	<b>\$ 126,531</b>	<b>\$ 251,391</b>	<b>\$ 710,643</b>

- (1) For purposes of this table, interest has been estimated based on interest rates in effect for our indebtedness as of December 27, 2018, and estimated borrowing levels in the future. Actual borrowing levels and interest costs may differ.
- (2) We enter into operating leases during the normal course of business. Most lease arrangements provide us with the option to renew the leases at defined terms. The future operating lease obligations would change if we were to exercise these options, or if we were to enter into additional operating leases.
- (3) Purchase obligations include all legally binding contracts such as firm commitments for inventory purchases, container commitments, software and license commitments and legally binding service contracts. Purchase orders that are not binding agreements are excluded from the table above.

### Off-Balance Sheet Arrangements

For fiscal 2018, except for operating leases entered into in the normal course of business, we were not party to any material off-balance sheet arrangements that are reasonably likely to have a current or future effect on our financial condition, net sales, expenses, results of operations, liquidity, capital expenditures or capital resources. We do not have any relationship with unconsolidated entities or financial partnerships for the purpose of facilitating off-balance sheet arrangements or for other contractually narrow or limited purposes.

### Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions about future events that affect amounts reported in our consolidated financial statements and related notes, as well as the related disclosure of contingent assets and liabilities at the date of the financial statements. Management evaluates its accounting policies, estimates and judgments on an ongoing basis. Management bases its estimates and judgments on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ under different assumptions and conditions, and such differences could be material to the consolidated financial statements.

Management evaluated the development and selection of its critical accounting policies and estimates and believes that the following involve a higher degree of judgment or complexity and are the most significant to reporting our results of operations and financial position, and are therefore discussed as critical. The following critical accounting policies reflect the significant estimates and judgments used in the preparation of our consolidated financial statements. With respect to critical accounting policies, even a relatively minor variance between actual and expected experience can potentially have a materially favorable or unfavorable impact on subsequent results of operations. More information on all of our significant account policies can be found in “Note 1.—Summary of Significant Accounting Policies” to our audited consolidated financial statements included elsewhere in this filing.

#### *Revenue Recognition*

We recognize revenue and the related cost of sales when we satisfy the performance obligations in contracts with our customers. Our performance obligations for our retail store sales as well as for orders placed through our website and shipped to our

customers are satisfied at the point-of-sale, which is the point at which the customer obtains control of the inventory as described under Accounting Standards Update (ASU) No. 2014-09, "Revenue from Contracts with Customers" (Topic 606). Shipping and handling activities are performed after the customer obtains control of the goods and are accounted for as activities to fulfill the promise to transfer goods, rather than a separate performance obligation as outlined within Topic 606. Payment is due from the customer immediately at the point-of-sale for both retail store sales and website sales. The nature of the goods offered include hard surface flooring and related accessories. We do not perform installation services, and we offer free design services in-store. The transaction price recognized in revenues represents the selling price of the products offered. Sales taxes collected are not recognized as revenue as these amounts are ultimately remitted to the appropriate taxing authorities.

Our customers have the right to return the goods sold to them within a reasonable period, typically ninety days. The right of return is an element of variable consideration as defined within Topic 606. We reserve for future returns of previously sold goods based on historical experience and various other assumptions that we believe to be reasonable. This reserve reduces sales and cost of sales as well as establishes a return asset and refund liability as defined with Topic 606. For the fiscal year ended December 27, 2018, the return asset is included within Prepaid expenses and other current assets and the refund liability is included within Accrued expenses and other current liabilities, each respectively on the Consolidated Balance Sheets. We adopted the standard using the modified retrospective transition method within Topic 606; therefore, we accounted for the return asset and all provisions of Topic 606 prospectively. The return asset is included in Inventories, net on the December 28, 2017 Consolidated Balance Sheets. The refund liability under Topic 605 and Topic 606 is included within Accrued expenses and other current liabilities. Merchandise exchanges of similar product and price are not considered merchandise returns and, therefore, are excluded when calculating the sales returns reserve.

#### ***Gift Cards and Merchandise Credits***

We sell gift cards to our customers in our stores and through our website and issue merchandise credits in our stores. We account for the programs by recognizing a liability at the time the gift card is sold or the merchandise credit is issued. The liability is relieved and revenue is recognized upon redemption. Additionally, we recognize breakage income in proportion to the pattern of rights exercised by the customer when we expect to be entitled to breakage. Net sales related to the estimated breakage are included in net sales in the consolidated statement of income. We have an agreement with an unrelated third-party who is the issuer of our gift cards and also assumes the liability for unredeemed gift cards. We are not subject to claims under unclaimed property statutes, as the agreement effectively transfers the ownership of such unredeemed gift cards and the related future escheatment liability, if any, to the third-party. Accordingly, gift card breakage income of \$1,584 thousand, \$757 thousand, and \$627 thousand was recognized in fiscal 2018, fiscal 2017, and fiscal 2016, respectively, for such unredeemed gift cards.

#### ***Inventory Valuation and Shrinkage***

Inventories consist of merchandise held for sale and are stated at the lower of cost and net realizable value. When evidence exists that the net realizable value of inventory is lower than its cost, the difference is recorded in cost of sales in the consolidated statement of income as a loss in the period in which it occurs. We determine inventory costs using the weighted average cost method. We capitalize transportation, duties and other costs to get product to our retail locations. We provide provisions for losses related to shrinkage and other amounts that are otherwise not expected to be fully recoverable. These provisions are calculated based on historical shrinkage, selling price, margin and current business trends. The estimates have calculations that require management to make assumptions based on the current rate of sales, age, salability and profitability of inventory, historical percentages that can be affected by changes in our merchandising mix, customer preferences, rates of sell through and changes in actual shrinkage trends. We do not believe there is a reasonable likelihood that there will be a material change in the assumptions we use to calculate our inventory provisions. However, if actual results are not consistent with our estimates and assumptions, we may be exposed to losses or gains that could be material.

#### ***Geographic Regions and Reporting Segments***

We have identified each of the eight geographic regions (the Pacific, Southwest, Midwest, Southeast, Gulf, Mid South, Mid Atlantic, and Northeast) of our operating segment as separate components and have determined that these components have similar economic characteristics and therefore should be aggregated into one reporting unit. We reached this conclusion based on the level of similarity of a number of quantitative and qualitative factors, including net sales, gross profit margin, the manner in which we operate our business, the similarity of hard surface flooring products, operating procedures, marketing initiatives, store layout, employees, customers and methods of distribution, as well as the level of shared resources between the components.

## Recently Issued Accounting Pronouncements

In January 2017, the FASB issued ASU No. 2017-04, *"Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment."* This standard simplifies how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. ASU No. 2017-04 is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years, with early adoption permitted after January 1, 2017. The Company elected to early adopt this standard during the fourth quarter of 2017. The amendments in this update should be applied using a prospective approach. The adoption of ASU No. 2017-04 did not have a material impact on our Consolidated Financial Statements.

In October 2016, the FASB issued ASU No. 2016-16, *"Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory."* This standard update requires an entity to recognize the income tax consequences of intra-entity transfers of assets other than inventory when the transfer occurs. ASU No. 2016-16 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption permitted. The amendments in this update should be applied using a modified retrospective approach. The adoption of ASU No. 2016-16 in the first quarter of 2018 did not have a material impact on our Consolidated Financial Statements.

In August 2016, the FASB issued ASU No. 2016-15, *"Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments."* The standard update addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU No. 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption permitted. The amendments in this update should be applied using a retrospective approach. The adoption of ASU No. 2016-15 in the first quarter of fiscal 2018 did have a material impact on our Consolidated Statements of Cash Flows.

In March 2016, the FASB issued ASU No. 2016-09, *"Compensation—Stock Compensation (Topic 718): Improvements to Employees Share-Based Payment Accounting."* The update is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. The amendments in this update are effective for fiscal years beginning after December 15, 2016, and interim periods within those years, with early adoption permitted. Depending on the amendment, methods used to apply the requirements of the update include modified retrospective, retrospective, and prospective. We elected to early adopt this standard during the second quarter of 2016. The net cumulative effect of this change was recognized as a \$148 thousand reduction to retained earnings and the recognition of \$238 thousand of additional paid-in capital. The adoption of this standard resulted in a modified retrospective adjustment on our Consolidated Balance Sheet as of January 1, 2016, the beginning of the annual period that includes the interim period of adoption.

In February 2016, the FASB issued ASU No. 2016-02, *"Leases (Topic 842)."* ASU No. 2016-02 requires that lessees recognize lease assets and lease liabilities for all leases with greater than 12 month terms on the balance sheet. The guidance also requires disclosures about the amount, timing and uncertainty of cash flows arising from leases. This new guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within those years, with early adoption permitted. We will adopt the ASU in the first quarter of our fiscal year 2019, using the modified retrospective approach. We also plan to elect the package of practical expedients to use in transition, which permits us not to reassess under the new standard our prior conclusions about lease identification and lease classification. We will utilize our lease accounting software to facilitate implementation that will retain the lease classification and initial direct costs for any leases that exist prior to adoption of the standard. We have performed procedures to evaluate the landscape of our real estate, personal property and other arrangements that may meet the definition of a lease. Based on these efforts, we expect that the adoption will result in a significant increase to our long-term assets and liabilities as, at a minimum, substantially all of our current lease commitments will be subject to balance sheet recognition. We do not expect the adoption to have a material impact to our Consolidated Statements of Income or Statements of Cash Flows.

In July 2015, the FASB issued ASU No. 2015-11, *"Inventory (Topic 330): Simplifying the Measurement of Inventory."* ASU No. 2015-11 provides new guidance for entities using first-in, first-out or average cost to simplify the subsequent measurement of inventory, which proposes that inventory should be measured at the lower of cost and net realizable value. Net realizable value is defined as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. This guidance eliminates the option to subsequently measure inventory at replacement cost or net realizable value less an approximately normal profit margin. This new guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within those years. The amendments in this update should be applied prospectively. The adoption of ASU No. 2015-11 did not have a material impact on our Consolidated Financial Statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*." ASU No. 2014-09 provides new guidance related to the core principle that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to receive in exchange for those goods or services provided. We adopted this standard using the modified retrospective approach in the first quarter of fiscal 2018, effective December 29, 2017. Under the new guidance, we recognize revenue at the time the customer obtains control of the inventory. The cumulative adjustment upon adoption primarily resulted in a reduction of deferred revenue and related inventories and an increase to retained earnings of \$7.8 million, net of tax. The adoption of ASU No. 2014-09 did not have a material impact to the Company's Consolidated Financial Statements.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Market risk represents the risk of changes in the value of market risk sensitive instruments caused by fluctuations in foreign exchange rates, interest rates and commodity prices. Changes in these factors could cause fluctuations in the results of our operations and cash flows. In the ordinary course of business, we are primarily exposed to foreign currency, interest rate risks and risks from the impact of inflation or deflation.

***Foreign Currency Risk***

We contract for production with third parties primarily in Asia and Europe. While substantially all of these contracts are stated in U.S. dollars, there can be no assurance that the cost for the future production of our products will not be affected by exchange rate fluctuations between the U.S. dollar and the local currencies of these contractors. Due to the number of currencies involved, we cannot quantify the potential impact of future currency fluctuations on net income (loss) in future years. To date, such exchange fluctuations have not had a material impact on our financial condition or results of operations.

***Interest Rate Risk***

Our operating results are subject to risk from interest rate fluctuations on our Credit Facilities, which carry variable interest rates. As of December 27, 2018, our outstanding variable rate debt aggregated approximately \$149.0 million. Based on December 27, 2018 debt levels, an increase or decrease of 1% in the effective interest rate would cause an increase or decrease in interest cost of approximately \$1.5 million over the next twelve months. To lessen our exposure to changes in interest rate risk, we entered into two separate \$102.5 million interest rate cap agreements in November 2016 with Bank of America and Wells Fargo that capped our LIBOR at 2.0% beginning in December 2016.

Additionally, in July 2017, the Financial Conduct Authority (the authority that regulates LIBOR) announced it intends to stop compelling banks to submit rates for the calculation of LIBOR after 2021. The Alternative Reference Rates Committee ("ARRC") has proposed that the Secured Overnight Financing Rate ("SOFR") is the rate that represents best practice as the alternative to USD-LIBOR for use in derivatives and other financial contracts that are currently indexed to USD-LIBOR. ARRC has proposed a paced market transition plan to SOFR from USD-LIBOR and organizations are currently working on industry wide and company specific transition plans as it relates to derivatives and cash markets exposed to USD-LIBOR. The Company has material contracts that are indexed to USD-LIBOR and is monitoring this activity and evaluating the related risks.

***Impact of Inflation/Deflation***

We do not believe that inflation has had a material impact on our net sales or operating results for the past three fiscal years. However, substantial increases in costs, including the price of raw materials, labor, energy and other inputs used in the production of our merchandise, could have a significant impact on our business and the industry in the future. Additionally, while deflation could positively impact our merchandise costs, it could have an adverse effect on our average unit retail price, resulting in lower net sales and operating results.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA .**

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders of  
Floor & Decor Holdings, Inc. and Subsidiaries

**Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Floor & Decor Holdings, Inc. and Subsidiaries (the Company) as of December 27, 2018 and December 28, 2017, the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 27, 2018, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 27, 2018 and December 28, 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 27, 2018, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 27, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated February 25, 2019, expressed an adverse opinion thereon.

**Basis for Opinion**

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 2011.

Atlanta, Georgia

February 25, 2019

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders of  
Floor & Decor Holdings, Inc. and Subsidiaries

**Opinion on Internal Control Over Financial Reporting**

We have audited Floor & Decor Holdings, Inc. and Subsidiaries' internal control over financial reporting as of December 27, 2018, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, because of the effect of the material weakness described below on the achievement of the objectives of the control criteria, Floor & Decor Holdings, Inc. and Subsidiaries (the Company) has not maintained effective internal control over financial reporting as of December 27, 2018, based on the COSO criteria.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weakness has been identified and included in management's assessment.

Management has identified a material weakness in controls related to information technology general controls (ITGCs) in the areas of user access and program change management over certain information technology (IT) systems and the reports generated from these systems used in the execution of controls that support the Company's financial reporting processes. As a result, business process automated and manual controls that were dependent on the affected ITGCs could have been adversely impacted.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of Floor & Decor Holdings, Inc. and Subsidiaries' as of December 27, 2018 and December 28, 2017, the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 27, 2018, and the related notes. This material weakness was considered in determining the nature, timing and extent of audit tests applied in our audit of the 2018 consolidated financial statements, and this report does not affect our report dated February 25, 2019, which expressed an unqualified opinion thereon.

**Basis for Opinion**

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

**Definition and Limitations of Internal Control Over Financial Reporting**

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP

Atlanta, Georgia

February 25, 2019

**Floor & Decor Holdings, Inc. and Subsidiaries**  
**Consolidated Balance Sheets**  
(In Thousands, Except Share and Per Share Data)

	As of December 27, 2018	As of December 28, 2017
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 644	\$ 556
Income taxes receivable	4,324	12,472
Receivables, net	67,527	54,041
Inventories, net	471,014	427,950
Prepaid expenses and other current assets	15,949	8,193
<b>Total current assets</b>	<b>559,458</b>	<b>503,212</b>
Fixed assets, net	328,366	220,952
Intangible assets, net	109,330	109,362
Goodwill	227,447	227,447
Other assets	9,490	7,019
<b>Total long-term assets</b>	<b>674,633</b>	<b>564,780</b>
<b>Total assets</b>	<b>\$ 1,234,091</b>	<b>\$ 1,067,992</b>
<b>Liabilities and stockholders' equity</b>		
Current liabilities:		
Current portion of term loans	\$ 3,500	\$ 3,500
Trade accounts payable	313,503	258,730
Accrued expenses and other current liabilities	82,038	74,547
Deferred revenue	5,244	22,523
<b>Total current liabilities</b>	<b>404,285</b>	<b>359,300</b>
Term loans	141,834	144,562
Revolving line of credit	—	41,000
Deferred rent	36,980	25,570
Deferred income tax liabilities, net	26,838	27,218
Tenant improvement allowances	37,295	26,779
Other liabilities	2,550	703
<b>Total long-term liabilities</b>	<b>245,497</b>	<b>265,832</b>
<b>Total liabilities</b>	<b>649,782</b>	<b>625,132</b>
Commitments and contingencies (Note 9)		
<b>Stockholders' equity</b>		
Capital stock:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized; 0 shares issued and outstanding at December 27, 2018 and December 28, 2017	—	—
Common stock Class A, \$0.001 par value; 450,000,000 shares authorized; 97,588,539 shares issued and outstanding at December 27, 2018 and 95,509,179 issued and outstanding at December 28, 2017	98	96
Common stock Class B, \$0.001 par value; 10,000,000 shares authorized; 0 shares issued and outstanding at December 27, 2018 and December 28, 2017	—	—
Common stock Class C, \$0.001 par value; 30,000,000 shares authorized; 0 shares issued and outstanding at December 27, 2018 and December 28, 2017	—	—
Additional paid-in capital	340,462	323,419
Accumulated other comprehensive income (loss), net	186	(205)
Retained earnings	243,563	119,550
<b>Total stockholders' equity</b>	<b>584,309</b>	<b>442,860</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 1,234,091</b>	<b>\$ 1,067,992</b>

See accompanying notes to consolidated financial statements.

**Floor & Decor Holdings, Inc. and Subsidiaries**  
**Consolidated Statements of Income**  
**(In Thousands, Except Per Share Data)**

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
Net sales	\$ 1,709,848	\$ 1,384,767	\$ 1,050,759
Cost of sales	1,007,580	812,203	621,497
Gross profit	702,268	572,564	429,262
Operating expenses:			
Selling and store operating	439,495	353,647	271,876
General and administrative	105,327	84,661	64,025
Pre-opening	26,145	16,485	13,732
Litigation settlement	—	—	10,500
Total operating expenses	570,967	454,793	360,133
Operating income	131,301	117,771	69,129
Interest expense	8,917	13,777	12,803
Loss on early extinguishment of debt	—	5,442	1,813
Income before income taxes	122,384	98,552	54,513
Provision for income taxes	6,197	(4,236)	11,474
Net income	\$ 116,187	\$ 102,788	\$ 43,039
Basic earnings per share	\$ 1.20	\$ 1.13	\$ 0.52
Diluted earnings per share	\$ 1.11	\$ 1.03	\$ 0.49

See accompanying notes to consolidated financial statements.

**Floor & Decor Holdings, Inc. and Subsidiaries**  
**Consolidated Statements of Comprehensive Income**  
**(In Thousands)**

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
Net income	\$ 116,187	\$ 102,788	\$ 43,039
Other comprehensive income (loss) —change in fair value of hedge instruments, net of tax	391	(381)	276
<b>Total comprehensive income</b>	<b>\$ 116,578</b>	<b>\$ 102,407</b>	<b>\$ 43,315</b>

See accompanying notes to consolidated financial statements.

**Floor & Decor Holdings, Inc. and Subsidiaries**  
**Consolidated Statements of Stockholders' Equity**  
(In Thousands)

	Preferred Stock		Common Stock Class A		Common Stock Class B		Common Stock Class C		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount				
Balance, December 31, 2015	—	\$ —	76,847	\$ 77	251	\$ —	6,275	\$ 6	\$ 264,288	\$ (100)	\$ 48,094	\$ 312,365
Stock based compensation expense	—	—	—	—	—	—	—	—	3,182	—	47	3,229
Exercise of stock options	—	—	—	—	145	—	—	—	284	—	—	284
Other comprehensive gain, net of tax	—	—	—	—	—	—	—	—	—	276	—	276
Dividend declared	—	—	—	—	—	—	—	—	(150,722)	—	(74,278)	(225,000)
Cumulative effect from adoption of ASU No. 2016-09	—	—	—	—	—	—	—	—	238	—	(148)	90
Net income	—	—	—	—	—	—	—	—	—	—	43,039	43,039
Balance, December 29, 2016	—	—	76,847	77	396	—	6,275	6	117,270	176	16,754	134,283
Stock based compensation expense	—	—	—	—	—	—	—	—	4,951	—	8	4,959
Conversion of Class B Common Stock	—	—	396	—	(396)	—	—	—	—	—	—	—
Conversion of Class C Common Stock	—	—	6,275	6	—	—	(6,275)	(6)	—	—	—	—
Exercise of stock options	—	—	1,828	2	—	—	—	—	8,872	—	—	8,874
IPO proceeds	—	—	10,147	10	—	—	—	—	192,326	—	—	192,336
Issuance of restricted stock awards	—	—	15	—	—	—	—	—	—	—	—	—
Other comprehensive loss, net of tax	—	—	—	—	—	—	—	—	—	(381)	—	(381)
Net income	—	—	—	—	—	—	—	—	—	—	102,788	102,788
Balance, December 28, 2017	—	—	95,509	96	—	—	—	—	323,419	(205)	119,550	442,860
Stock based compensation expense	—	—	—	—	—	—	—	—	6,514	—	—	6,514
Exercise of stock options	—	—	2,069	2	—	—	—	—	10,529	—	—	10,531
Issuance of restricted stock awards	—	—	10	—	—	—	—	—	—	—	—	—
Cumulative effect from adoption of ASU No. 2016-09	—	—	—	—	—	—	—	—	—	—	7,826	7,826
Other comprehensive gain (loss), net of tax	—	—	—	—	—	—	—	—	—	391	—	391
Net income	—	—	—	—	—	—	—	—	—	—	116,187	116,187
Balance, December 27, 2018	—	\$ —	97,588	\$ 98	—	\$ —	—	\$ —	\$ 340,462	\$ 186	\$ 243,563	\$ 584,309

See accompanying notes to consolidated financial statements.

**Floor & Decor Holdings, Inc. and Subsidiaries**  
**Consolidated Statements of Cash Flows**  
(In Thousands)

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
<b>Operating activities</b>			
Net income	\$ 116,187	\$ 102,788	\$ 43,039
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	51,992	38,062	28,604
Non-cash loss on early extinguishment of debt	—	5,442	1,813
Loss on asset disposals	23	128	451
Amortization of tenant improvement allowances	(4,494)	(3,311)	(2,561)
Deferred income taxes	(968)	(557)	(5,536)
Interest cap derivative contracts	(212)	—	—
Stock based compensation expense	6,514	4,959	3,229
Changes in operating assets and liabilities:			
Receivables, net	(13,486)	(19,508)	(10,793)
Inventories, net	(53,557)	(134,248)	(21,133)
Other assets	(9,921)	(1,591)	(4,817)
Trade accounts payable	54,773	100,264	11,145
Accrued expenses and other current liabilities	(1,731)	9,485	27,244
Income taxes	6,221	(18,259)	8,271
Deferred revenue	3,002	8,067	2,311
Deferred rent	14,455	9,243	3,870
Tenant improvement allowances	15,010	7,984	4,244
Other	1,816	259	75
Net cash provided by operating activities	185,624	109,207	89,456
<b>Investing activities</b>			
Purchases of fixed assets	(151,397)	(102,253)	(74,648)
Net cash used in investing activities	(151,397)	(102,253)	(74,648)
<b>Financing activities</b>			
Borrowings on revolving line of credit	217,050	236,700	171,850
Payments on revolving line of credit	(258,050)	(245,700)	(214,750)
Proceeds from term loans	—	—	362,000
Payments on term loans	(3,500)	(197,500)	(98,334)
Prepayment penalty on term loan extinguishment	—	—	(179)
Net proceeds from initial public offering	—	192,336	—
Proceeds from exercise of stock options	10,531	8,874	284
Debt issuance costs	(170)	(1,559)	(10,546)
Cash dividends	—	—	(225,000)
Net cash used in financing activities	(34,139)	(6,849)	(14,675)
Net increase in cash and cash equivalents	88	105	133
Cash and cash equivalents, beginning of the period	556	451	318
Cash and cash equivalents, end of the period	\$ 644	\$ 556	\$ 451
<b>Supplemental disclosures of cash flow information</b>			
Cash paid for interest	\$ 7,563	\$ 15,748	\$ 6,922
Cash paid for income taxes	\$ 1,082	\$ 14,392	\$ 8,929
Fixed assets accrued at the end of the period	\$ 15,120	\$ 8,521	\$ 5,387
Fixed assets acquired as part of lease - paid for by lessor	\$ —	\$ 1,786	\$ 2,290

See accompanying notes to consolidated financial statements.



Floor & Decor Holdings, Inc. and Subsidiaries  
Notes to Consolidated Financial Statements  
December 27, 2018

**1. Summary of Significant Accounting Policies**

***Nature of Business***

Floor & Decor Holdings, Inc. (f/k/a FDO Holdings, Inc.), together with its subsidiaries (the “Company,” “we,” “our” or “us”) is a highly differentiated, rapidly growing specialty retailer of hard surface flooring and related accessories. We offer a broad in-stock assortment of tile, wood, laminate, vinyl, and natural stone flooring along with decorative and installation accessories at everyday low prices. Our stores appeal to a variety of customers, including professional installers and commercial businesses (“Pro”), Do It Yourself customers (“DIY”) and customers who buy the products for professional installation (“Buy it Yourself” or “BIY”). We operate within one reportable segment.

As of December 27, 2018, the Company, through its wholly owned subsidiary, Floor and Decor Outlets of America, Inc. (“F&D”), operates 100 warehouse-format stores, which average 75,000 square feet, and one small-format standalone design center in 28 states, as well as three distribution centers and an e-commerce site, FloorandDecor.com.

***Fiscal Year***

The Company’s fiscal year is the 52- or 53-week period ending on the Thursday on or preceding December 31st. Fiscal years ended December 27, 2018 (“fiscal 2018”), December 28, 2017 (“fiscal 2017”), and December 29, 2016 (“fiscal 2016”) include 52 weeks. When a 53-week fiscal year occurs, we report the additional week at the end of the fiscal fourth quarter. 52-week fiscal years consist of thirteen-week periods in the first, second, third and fourth quarters of the fiscal year.

***Basis of Presentation***

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”). The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. Unless indicated otherwise, the information in this Annual Report has been adjusted to give effect to a 321.820-for-one stock split of the Company’s outstanding common stock, which was approved by the Company’s board of directors and shareholders on April 13, 2017 and effected on April 24, 2017.

***Cash and Cash Equivalents***

Cash consists of currency and demand deposits with banks.

***Receivables***

Receivables consist primarily of amounts due from credit card companies, receivables from vendors and tenant improvement allowances owed by landlords. The Company typically collects its credit card receivables within three to five business days of the underlying sale to the customer. The Company has agreements with a majority of its large merchandise vendors that allow for specified rebates based on purchasing volume. Generally, these agreements are on an annual basis, and the Company collects the rebates subsequent to its fiscal year end. Additionally, the Company has agreements with substantially all vendors that allow for the return of certain merchandise throughout the normal course of business. When inventory is identified to return to a vendor, it is removed from inventory and recorded as a receivable on the Consolidated Balance Sheet, and any variance between capitalized inventory cost associated with the return and the expected vendor reimbursement is expensed in Cost of sales in the Consolidated Statement of Income when the inventory is identified to be returned to the vendor. The Company reserves for estimated uncollected receivables based on historical trends, which historically have been immaterial. The allowance for doubtful accounts as of December 27, 2018 and December 28, 2017, was \$184 thousand and \$349 thousand, respectively.

**Credit Program**

Credit is offered to the Company's customers through a proprietary credit card underwritten by third-party financial institutions and at no recourse to the Company. Beginning in fiscal 2018, the Company began offering limited credit to its commercial clients. The total exposure at the end of fiscal 2018 was \$251 thousand.

**Inventory Valuation and Shrinkage**

Inventories consist of merchandise held for sale and are stated at the lower of cost and net realizable value. When evidence exists that the net realizable value of inventory is lower than its cost, the difference is recorded in Cost of sales in the Consolidated Statement of Income as a loss in the period in which it occurs. The Company determines inventory costs using the weighted average cost method. The Company capitalizes transportation, duties and other costs to get product to its retail locations. The Company records reserves for estimated losses related to shrinkage and other amounts that are otherwise not expected to be fully recoverable. These reserves are calculated based on historical shrinkage, selling price, margin and current business trends. The estimates have calculations that require management to make assumptions based on the current rate of sales, age, salability and profitability of inventory, historical percentages that can be affected by changes in the Company's merchandising mix, customer preferences and changes in actual shrinkage trends. These reserves totaled \$4,265 thousand and \$2,936 thousand as of December 27, 2018 and December 28, 2017, respectively.

Physical inventory counts and cycle counts are performed on a regular basis in each store and distribution center to ensure that amounts reflected in the accompanying Consolidated Balance Sheets are properly stated. During the period between physical inventory counts in our stores, the Company accrues for estimated losses related to shrinkage on a store-by-store basis. Shrinkage is the difference between the recorded amount of inventory and the physical inventory. Shrinkage may occur due to theft or loss, among other things.

**Fixed Assets**

Fixed assets consist primarily of furniture, fixtures and equipment, leasehold improvements (including those that are reimbursed by landlords as tenant improvement allowances), computer software and hardware and land. Fixed assets are stated at cost less accumulated depreciation utilizing the straight-line method over the assets' estimated useful lives.

Leasehold improvements are amortized using the straight-line method over the shorter of (i) the original term of the lease, (ii) renewal term of the lease if the renewal is reasonably expected or (iii) the useful life of the improvement. The Company's fixed assets are depreciated using the following estimated useful lives:

	<b>Useful Life</b>
Furniture, fixtures and equipment	2 - 7 years
Leasehold improvements	10 - 25 years
Computer software and hardware	3 - 7 years
Land	Indefinite

The cost and related accumulated depreciation of assets sold or otherwise disposed are removed from the accounts, and the related gain or loss is reported in the Consolidated Statements of Income.

**Capitalized Software Costs**

The Company capitalizes certain costs related to the acquisition and development of software and amortizes these costs using the straight-line method over the estimated useful life of the software. Certain development costs not meeting the criteria for capitalization are expensed as incurred.

**Goodwill and Other Indefinite-Lived Intangible Assets**

Goodwill represents the excess of purchase price over the fair value of net assets acquired. The Company does not amortize goodwill and other intangible assets with indefinite lives resulting from business combinations but, in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 350, *Intangibles—Goodwill and Other*, does

assess the recoverability of goodwill annually in the fourth quarter of each fiscal year, or more often if indicators warrant, by determining whether the fair value of the reporting unit exceeds its carrying value. In accordance with ASC 350, identifiable intangible assets with finite lives are amortized over their estimated useful lives. Each year the Company may assess qualitative factors to determine whether it is more likely than not that the fair value of the single reporting unit is less than its carrying amount as a basis for determining whether it is necessary to complete quantitative impairment assessments.

The Company completed a qualitative assessment in fiscal 2018. Based on such goodwill impairment analysis performed qualitatively as of October 26, 2018, the Company determined that the fair value of its reporting unit is in excess of the carrying value. No events or changes in circumstances have occurred since the date of the Company's most recent annual impairment test that would more likely than not reduce the fair value of the reporting unit below its carrying amount.

The Company annually (or more frequently if there are indicators of impairment) evaluates whether its indefinite-lived asset continues to have an indefinite life or have impaired carrying values due to changes in the asset or its related risks. The impairment review is performed by comparing the carrying value of the indefinite-lived intangible asset to its estimated fair value. If the recorded carrying value of the indefinite-lived asset exceeds its estimated fair value, an impairment charge is recorded to write the asset down to its estimated fair value.

The estimated lives of the Company's intangible assets are as follows:

	<b>Useful Life</b>
Trade names	Indefinite
Vendor relationships	10 years

The Company's goodwill and other indefinite-lived intangible assets impairment loss calculations contain uncertainties because they require management to make significant judgments in estimating the fair value of the Company's reporting unit and indefinite-lived intangible asset, including the projection of future cash flows, assumptions about which market participants are the most comparable, the selection of discount rates and the weighting of the income and market approaches. These calculations contain uncertainties because they require management to make assumptions such as estimating economic factors and the profitability of future business operations and, if necessary, the fair value of the reporting unit's assets and liabilities among others. Further, the Company's ability to realize the future cash flows used in its fair value calculations is affected by factors such as changes in economic conditions, changes in the Company's operating performance and changes in the Company's business strategies. Significant changes in any of the assumptions involved in calculating these estimates could affect the estimated fair value of the Company's reporting unit and indefinite-lived intangible assets and could result in impairment charges in a future period.

#### ***Long-Lived Assets***

Long-lived assets, such as fixed assets and intangible assets with finite lives, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Conditions that may indicate impairment include, but are not limited to, a significant adverse change in customer demand or business climate that could affect the value of an asset, a product recall or an adverse action by a regulator. If the sum of the estimated undiscounted future cash flows related to the asset is less than the asset's carrying value, the Company recognizes a loss equal to the difference between the carrying value and the fair value, usually determined by the estimated discounted cash flow analysis of the asset.

Since there is typically no active market for the Company's definite-lived intangible asset, the Company estimates fair value based on expected future cash flows at the time they are identified. The Company estimates future cash flows based on store-level historical results, current trends and operating and cash flow projections. The Company amortizes the asset with a finite life over its estimated useful life on a straight-line basis. This amortization methodology best matches the pattern of economic benefit that is expected from the definite-lived intangible asset. The Company evaluates the useful life of its intangible asset on an annual basis.

#### ***Tenant Improvement Allowances and Deferred Rent***

The Company accounts for tenant improvement allowances and deferred rent as liabilities or assets on the balance sheet. Tenant improvement allowances are amounts received from a lessor for improvements to leased properties and are amortized against rent expense over the life of the respective leases. Fixed rents are recognized ratably over the initial non-cancellable lease term.

Deferred rent represents differences between the actual cash paid for rent and the amount of straight-line rent over the initial non-cancellable term.

#### ***Self-Insurance Reserves***

The Company is partially self-insured for workers' compensation and general liability claims less than certain dollar amounts and maintains insurance coverage with individual and aggregate limits. The Company also has a basket aggregate limit to protect against losses exceeding \$8.6 million (subject to adjustment and certain exclusions) for workers' compensation claims and general liability claims. The Company's liabilities represent estimates of the ultimate cost for claims incurred, including loss adjusting expenses, as of the balance sheet date. The estimated liabilities are not discounted and are established based upon analysis of historical data, actuarial estimates, regulatory requirements, an estimate of claims incurred but not yet reported and other relevant factors. Management utilizes independent third-party actuarial studies to help assess the liability on a regular basis.

#### ***Commitments and Contingencies***

Liabilities for loss contingencies arising from claims, assessments, litigation, fines, penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

#### ***Asset Retirement Obligations***

An asset retirement obligation ("ARO") represents a legal obligation associated with the retirement of a tangible long-lived asset that is incurred upon the acquisition, construction, development or normal operation of that long-lived asset. The Company's AROs are primarily associated with leasehold improvements that, at the end of a lease, the Company is contractually obligated to remove in order to comply with certain lease agreements. The ARO is recorded in Other long-term liabilities on the Consolidated Balance Sheets and will be subsequently adjusted for changes in fair value. The associated estimated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and depreciated over its useful life.

Changes in (i) inflation rates and (ii) the estimated costs, timing and extent of future store closure activities each result in (a) a current adjustment to the recorded liability and related asset and (b) a change in the liability and asset amounts to be recorded prospectively. Any changes related to the assets are then recognized in accordance with our depreciation policy, which would generally result in depreciation expense being recognized prospectively over the shorter of the remaining lease term or estimated useful life.

#### ***Fair Value Measurements—Debt***

The Company estimates fair values in accordance with ASC 820, *Fair Value Measurement*. ASC 820 provides a framework for measuring fair value and requires disclosures about fair value measurements. ASC 820 defines fair value as the price that would be received from the sale of an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. Additionally, ASC 820 defines levels within a hierarchy based upon observable and non-observable inputs.

- Level 1: Inputs that are quoted prices in active markets for identical assets or liabilities
- Level 2: Inputs other than quoted prices in active markets for assets or liabilities that are either directly or indirectly observable
- Level 3: Inputs that are non-observable that reflect the reporting entity's own assumptions

The fair values of certain of the Company's debt instruments have been determined by the Company utilizing Level 3 inputs, such as available market information and appropriate valuation methodologies, including the rates for similar instruments and the discounted cash flows methodology.

#### ***Derivative Financial Instruments***

The Company uses derivative financial instruments to maintain a portion of its long-term debt obligations at a targeted balance of fixed and variable interest rate debt to manage its risk associated with fluctuations in interest rates. We recognize derivative

contracts at fair value on our Consolidated Balance Sheets. The fair value is calculated utilizing Level 2 inputs. Unrealized changes in the fair value of hedged derivative instruments are recorded in Accumulated other comprehensive (loss) income within the equity section of our Consolidated Balance Sheets.

The effective portion of the gain or loss on the derivatives is reported as a component of Comprehensive income within the Consolidated Statements of Comprehensive Income and reclassified into earnings in the same period in which the hedged transaction affects earnings. The effective portion of the derivative represents the change in fair value of the hedge that offsets the change in fair value of the hedged item. To the extent changes in fair values of the instruments are not highly effective, the ineffective portion of the hedge is immediately recognized in earnings.

We perform an assessment of the effectiveness of our derivative contracts designated as hedges, including assessing the possibility of counterparty default. If we determine that a derivative is no longer expected to be highly effective, we discontinue hedge accounting prospectively and recognize subsequent changes in the fair value of the hedge in earnings. We believe our derivative contracts, which continue to be designated as cash flow hedges, and which consist of interest rate cap contracts, will continue to be highly effective in offsetting changes in cash flow attributable to floating interest rate risk. See footnote 8. *Derivatives and Risk Management* for additional information.

#### ***Use of Estimates***

The preparation of the financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amounts of fixed assets and intangibles, asset retirement obligations, allowances for accounts receivable and inventories, reserves for workers' compensation and general liability claims incurred but not reported and deferred income tax assets and liabilities. Actual results could differ from these estimates.

#### ***Revenue Recognition***

We recognize revenue and the related cost of sales when we satisfy the performance obligations in contracts with our customers. Our performance obligations for our retail store sales as well as for orders placed through our website and shipped to our customers are satisfied at the point-of-sale, which is the point at which the customer obtains control of the inventory as described under Accounting Standards Update (ASU) No. 2014-09, "Revenue from Contracts with Customers" (Topic 606). Shipping and handling activities are performed after the customer obtains control of the goods and are accounted for as activities to fulfill the promise to transfer goods, rather than a separate performance obligation as outlined within Topic 606. Payment is due from the customer immediately at the point-of-sale for both retail store sales and website sales. The nature of the goods offered include hard surface flooring and related accessories. We do not perform installation services, and we offer free design services in-store. The transaction price recognized in revenues represents the selling price of the products offered. Sales taxes collected are not recognized as revenue as these amounts are ultimately remitted to the appropriate taxing authorities.

Our customers have the right to return the goods sold to them within a reasonable period, typically 90 days. The right of return is an element of variable consideration as defined within Topic 606. We reserve for future returns of previously sold goods based on historical experience and various other assumptions that we believe to be reasonable. This reserve reduces sales and cost of sales as well as establishes a return asset and refund liability as defined with Topic 606. For the fiscal year ended December 27, 2018, the return asset is included within Prepaid expenses and other current assets and the refund liability is included within Accrued expenses and other current liabilities, each respectively on the Consolidated Balance Sheets. We adopted the standard using the modified retrospective transition method within Topic 606; therefore, we accounted for the return asset and all provisions of Topic 606 prospectively. The return asset is included in Inventories, net on the December 28, 2017 Consolidated Balance Sheets. The refund liability under Topic 605 and Topic 606 is included within Accrued expenses and other current liabilities. Merchandise exchanges of similar product and price are not considered merchandise returns and, therefore, are excluded when calculating the sales returns reserve.

#### ***Gift Cards and Merchandise Credits***

We sell gift cards to our customers in our stores and through our website and issue merchandise credits in our stores. We account for the programs by recognizing a liability at the time the gift card is sold or the merchandise credit is issued. The liability is

relieved and revenue is recognized upon redemption. Additionally, we recognize breakage income in proportion to the pattern of rights exercised by the customer when we expect to be entitled to breakage. Net sales related to the estimated breakage are included in net sales in the Consolidated Statement of Income. We have an agreement with an unrelated third-party who is the issuer of the Company's gift cards and also assumes the liability for unredeemed gift cards. The Company is not subject to claims under unclaimed property statutes, as the agreement effectively transfers the ownership of such unredeemed gift cards and the related future escheatment liability, if any, to the third-party. Gift card breakage is recognized based upon historical redemption patterns and represents the balance of gift cards for which the Company believes the likelihood of redemption by the customer is remote. Accordingly, in fiscal 2018, fiscal 2017, and fiscal 2016 gift card breakage income of \$1,584 thousand, \$757 thousand, and \$627 thousand was recognized in net sales in the Consolidated Statements of Income, respectively, for such unredeemed gift cards.

***Sales Returns and Allowances***

The Company accrues for estimated sales returns based on historical sales return results. The allowance for sales returns at December 27, 2018 and December 28, 2017, was \$8,335 thousand and \$7,189 thousand, respectively.

Merchandise exchanges of similar product and price are not considered merchandise returns and, therefore, are excluded when calculating the sales returns reserve.

***Cost of Sales***

Cost of sales consists of merchandise costs as well as freight to transport inventory to our distribution centers and stores, and duty and other costs that are incurred to distribute the merchandise to our stores. Cost of sales also includes shrinkage, damaged product disposals, distribution, warehousing, sourcing and compliance cost and arranging and paying for freight to deliver products to customers. The Company receives cash consideration from certain vendors related to vendor allowances and volume rebates, which is recorded as a reduction of costs of sales when the inventory is sold or as a reduction of the carrying value of inventory if the inventory is still on hand.

***Vendor Rebates and Allowances***

Vendor allowances consist primarily of volume rebates that are earned as a result of attaining certain inventory purchase levels and advertising allowances or incentives for the promotion of vendors' products. These vendor allowances are accrued, based on annual projections, as earned.

Vendor allowances earned are initially recorded as a reduction to the carrying value of inventory and a subsequent reduction in cost of sales when the related product is sold. Certain incentive allowances that are reimbursements of specific, incremental and identifiable costs incurred to promote vendors' products are recorded as an offset against these promotional expenses.

***Total Operating Expenses***

Total operating expenses consist primarily of store and administrative personnel wages and benefits, infrastructure expenses, supplies, fixed asset depreciation, store and corporate facility expenses, pre-opening costs, training and advertising costs. Credit card fees, insurance, personal property taxes, legal expenses and other miscellaneous operating costs are also included.

***Advertising***

The Company expenses advertising costs as the advertising takes place. Advertising costs incurred during the years ended December 27, 2018, December 28, 2017, and December 29, 2016, were \$55,283 thousand, \$43,560 thousand, and \$33,497 thousand respectively, and are included in Selling and store operating expenses and Pre-opening expenses in the accompanying Consolidated Statements of Income.

***Pre-Opening Expenses***

The Company accounts for non-capital operating expenditures incurred prior to opening a new store as "pre-opening" expenses in its Consolidated Statements of Income. The Company's pre-opening expenses begin on average three to six months in advance of a store opening or relocating due to, among other things, the amount of time it takes to prepare a store for its grand opening. Pre-opening expenses primarily include: advertising, rent, staff training, staff recruiting, utilities, personnel and equipment

rental. A store is considered to be relocated if it is closed temporarily and re-opened within the same primary trade area. Pre-opening expenses for the years ended December 27, 2018, December 28, 2017, and December 29, 2016, totaled \$26,145 thousand, \$16,485 thousand, and \$13,732 thousand, respectively.

#### ***Loss on Early Extinguishment of Debt***

On May 2, 2017, the Company completed its initial public offering (“IPO”), pursuant to which it sold an aggregate of 10,147,025 shares of Class A common stock, par value \$0.001 per share. The Company received aggregate net proceeds of approximately \$192.0 million after deducting underwriting discounts and commissions and other offering expenses. The Company used net proceeds from the IPO of approximately \$192.0 million to repay a portion of the amounts outstanding under the Term Loan Facility, including accrued and unpaid interest. The partial paydown resulted in a loss on extinguishment of debt in the amount of approximately \$5.4 million related to unamortized original issue discount and unamortized deferred debt issuance costs.

#### ***Stock-Based Compensation***

The Company accounts for employee stock options, restricted stock, and employee stock purchase plans in accordance with ASC 718, *Compensation – Stock Compensation*. The Company obtains independent third-party valuation studies to assist it with determining the grant date fair value of our stock price. Stock options are granted with exercise prices equal to or greater than the fair market value on the date of grant as authorized by the board of directors or compensation committee. Options granted have vesting provisions ranging from one to five years. Stock option grants are generally subject to forfeiture if employment terminates prior to vesting. The Company has selected the Black-Scholes option pricing model for estimating the grant date fair value of stock option awards granted. The Company bases the risk-free interest rate on the yield of a zero coupon U.S. Treasury security with a maturity equal to the expected life of the option from the date of the grant. The Company estimates the dividend yield to be zero as the Company does not intend to pay dividends in the future. The Company estimates the volatility of the share price of its common stock by considering the historical volatility of the stock of similar public entities. The Company considers a number of factors in determining the appropriateness of the public entities included in the volatility assumption, including the entity's life cycle stage, growth profile, size, financial leverage and products offered. Stock-based compensation cost is measured at the grant date based on the value of the award and is recognized as expense over the requisite service period based on the number of years for which the requisite service is expected to be rendered.

#### ***Income Taxes***

The Company accounts for income taxes under the liability method in accordance with ASC 740, *Income Taxes*, which requires the recognition of deferred tax assets and liabilities for the future tax consequences attributable to differences between the financial statement carrying amounts and tax basis of existing assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Changes in tax laws and rates could affect recorded deferred tax assets and liabilities in the future. The effect on deferred tax assets and liabilities of a change in tax laws or rates is recognized in the period that includes the enactment date of such a change.

The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which the associated temporary differences became deductible. On a quarterly basis, the Company evaluates whether it is more likely than not that its deferred tax assets will be realized in the future and concludes whether a valuation allowance must be established.

The Company includes any estimated interest and penalties on tax-related matters in income taxes payable and income tax expense. The Company accounts for uncertain tax positions in accordance with ASC 740. ASC 740-10 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements using a two-step process for evaluating tax positions taken, or expected to be taken, on a tax return. The Company may only recognize the tax benefit from an uncertain tax position if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement. Uncertain tax positions require determinations and estimated liabilities to be made based on provisions of the tax law, which may be subject to change or varying interpretation. The Company does not believe it has any material risks related to uncertain tax positions.

### **Recent Accounting Pronouncements**

In January 2017, the FASB issued ASU No. 2017-04, *"Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment."* This standard simplifies how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. ASU No. 2017-04 is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years, with early adoption permitted after January 1, 2017. The Company elected to early adopt this standard during the fourth quarter of 2017. The amendments in this update should be applied using a prospective approach. The adoption of ASU No. 2017-04 did not have a material impact on the Company's Consolidated Financial Statements.

In October 2016, the FASB issued ASU No. 2016-16, *"Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory."* This standard update requires an entity to recognize the income tax consequences of intra-entity transfers of assets other than inventory when the transfer occurs. ASU No. 2016-16 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption permitted. The amendments in this update should be applied using a modified retrospective approach. The adoption of ASU No. 2016-16 did not have a material impact on the Company's Consolidated Financial Statements.

In August 2016, the FASB issued ASU No. 2016-15, *"Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments."* The standard update addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU No. 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption permitted. The amendments in this update should be applied using a retrospective approach. The adoption of ASU No. 2016-15 did not have a material impact on the Company's Consolidated Statements of Cash Flows.

In March 2016, the FASB issued ASU No. 2016-09, *"Compensation—Stock Compensation (Topic 718): Improvements to Employees Share-Based Payment Accounting."* The update is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. The amendments in this update are effective for fiscal years beginning after December 15, 2016, and interim periods within those years, with early adoption permitted. Depending on the amendment, methods used to apply the requirements of the update include modified retrospective, retrospective, and prospective. The Company elected to early adopt this standard during the second quarter of 2016. The net cumulative effect of this change was recognized as a \$148 thousand reduction to retained earnings and the recognition of \$238 thousand of additional paid-in capital. The adoption of this standard resulted in a modified retrospective adjustment on the Company's Consolidated Balance Sheet as of January 1, 2016, the beginning of the annual period that includes the interim period of adoption.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." ASU No. 2016-02 requires that lessees recognize lease assets and lease liabilities for all leases with greater than 12 month terms on the balance sheet. The guidance also requires disclosures about the amount, timing and uncertainty of cash flows arising from leases. This new guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within those years, with early adoption permitted. We will adopt the ASU in the first quarter of our fiscal year 2019, using the modified retrospective approach. We also plan to elect the package of practical expedients to use in transition, which permits us not to reassess under the new standard our prior conclusions about lease identification and lease classification. We will utilize our lease accounting software to facilitate implementation that will retain the lease classification and initial direct costs for any leases that exist prior to adoption of the standard. We have performed procedures to evaluate the landscape of our real estate, personal property and other arrangements that may meet the definition of a lease. Based on these efforts, we expect that the adoption will result in a significant increase to our long-term assets and liabilities as, at a minimum, substantially all of our current lease commitments will be subject to balance sheet recognition. We do not expect the adoption to have a material impact to our Consolidated Statements of Income or Statements of Cash Flows.

In July 2015, the FASB issued ASU No. 2015-11, *"Inventory (Topic 330): Simplifying the Measurement of Inventory."* ASU No. 2015-11 provides new guidance for entities using first-in, first-out or average cost to simplify the subsequent measurement of inventory, which proposes that inventory should be measured at the lower of cost and net realizable value. Net realizable value is defined as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. This guidance eliminates the option to subsequently measure inventory at replacement cost or net realizable value less an approximately normal profit margin. This new guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within those years. The amendments in this update should be applied prospectively. The adoption of ASU No. 2015-11 did not have a material impact on the Company's Consolidated Financial Statements.



In May 2014, the FASB issued ASU No. 2014-09, “*Revenue from Contracts with Customers (Topic 606)*.” ASU No. 2014-09 provides new guidance related to the core principle that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to receive in exchange for those goods or services provided. We adopted this standard in the first quarter of fiscal 2018 using the modified retrospective approach, effective December 29, 2017. The cumulative adjustment upon adoption primarily resulted in a reduction of deferred revenue and related inventories and an increase to retained earnings of \$7.8 million, net of tax. The adoption of ASU No. 2014-09 did not have a material impact to the Company’s Consolidated Financial Statements.

## **2. Revenues**

### ***Adoption of ASC Topic 606, “Revenue from Contracts with Customers”***

On December 29, 2017, the Company adopted Topic 606 using the modified retrospective method applied to those contracts that were not completed as of December 29, 2017. Results for reporting periods beginning after December 28, 2017 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting under ASC 605, Revenue Recognition (Topic 605).

The Company recorded a net increase to opening retained earnings of \$7.8 million, net of tax, as of December 29, 2017 due to the cumulative impact of adopting Topic 606, with the impact primarily related to transactions for which it allows customers to store their merchandise at its retail stores for final delivery at a later date. The cumulative adjustment primarily resulted in a reduction of deferred revenue and related inventories and an increase to retained earnings. The impact to revenues as a result of applying Topic 606 was immaterial for the fiscal year ended December 27, 2018.

### ***Deferred Revenue***

Under Topic 605, the Company recognized revenue for certain transactions for which it allowed customers to store their merchandise at its retail stores for final delivery at a later date when both collection, or reasonable assurance of collection of payment and final delivery of the product had occurred. Under Topic 605, the amount of revenue for which final delivery of the product had not occurred for these transactions was reflected in the Deferred revenue caption on the Consolidated Balance Sheet as of December 28, 2017. Under Topic 606, the Company evaluated the bill-and-hold criteria, and now recognizes revenue at the point-of-sale, when the customer obtains control of the inventory. Amounts in Deferred revenue at period-end reflect orders for which the inventory is not currently ready for physical transfer to the customer.

### ***Gift Card Breakage***

Under Topic 605, gift card breakage income was recognized based upon historical redemption patterns. Under Topic 606, gift card breakage income is recognized in proportion to the pattern of rights exercised by the customer when the Company expects to be entitled to breakage. The amount of revenue related to gift card breakage income in the cumulative transition adjustment, and for the fiscal year ended December 27, 2018 was immaterial to the Consolidated Financial Statements.

### ***Disaggregated Revenue***

The Company operates as a specialty retailer of hard surface flooring and related accessories through retail stores located in the United States and through its website. The Company’s chief operating decision maker is its Chief Executive Officer who reviews the Company’s consolidated financial information for purposes of allocating resources and evaluating the Company’s financial performance. Accordingly, the Company concluded it has one reportable segment.

The following table presents the net sales of each major product category for each of the last three fiscal years (in thousands):

Product Category	Fiscal Year Ended					
	December 27, 2018		December 28, 2017		December 29, 2016	
	Net Sales	% of Net Sales	Net Sales	% of Net Sales	Net Sales	% of Net Sales
Tile	\$ 476,337	27 %	\$ 419,745	30 %	\$ 325,433	31 %
Decorative Accessories	325,139	19	257,684	19	188,371	18
Laminate / Luxury Vinyl Plank	316,109	18	208,238	15	131,447	12
Installation Materials and Tools	272,994	16	217,427	16	165,330	16
Wood	192,087	12	167,152	12	142,751	14
Natural Stone	113,565	7	104,670	8	90,866	9
Delivery and Other	13,617	1	9,851	—	6,561	—
Total	<u>\$ 1,709,848</u>	<u>100 %</u>	<u>\$ 1,384,767</u>	<u>100 %</u>	<u>\$ 1,050,759</u>	<u>100 %</u>

### 3. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following (in thousands):

	December 27, 2018	December 28, 2017
Accrued incentive compensation	\$ 12,473	\$ 17,218
Sales tax payable	12,046	9,171
Insurance reserve- incurred but not reported	8,229	6,390
Other	49,290	41,768
Accrued Expenses	<u>\$ 82,038</u>	<u>\$ 74,547</u>

### 4. Fixed Assets

Fixed assets as of December 27, 2018 and December 28, 2017, consisted of the following (in thousands):

	December 27, 2018	December 28, 2017
Furniture, fixtures and equipment	\$ 174,663	\$ 126,821
Leasehold improvements	216,461	141,174
Computer software and hardware	83,628	52,687
Land	5,297	4,976
Fixed assets, at cost	<u>480,049</u>	<u>325,658</u>
Less: accumulated depreciation and amortization	<u>151,683</u>	<u>104,706</u>
Fixed assets, net	<u>\$ 328,366</u>	<u>\$ 220,952</u>

Depreciation and amortization on fixed assets for the years ended December 27, 2018, December 28, 2017, and December 29, 2016, were \$50,478 thousand, \$36,255 thousand, and \$27,459 thousand, respectively.

## 5. Intangible Assets

The following summarizes the balances of identifiable intangible assets as of December 27, 2018 and December 28, 2017 (in thousands):

	December 27, 2018			December 28, 2017	
	Estimated Useful Lives	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible asset:					
Vendor relationships	10 years	\$ 319	\$ (258)	\$ 319	\$ (226)
Indefinite-lived intangible asset:					
Trade names		109,269	—	109,269	—
		<u>\$ 109,588</u>	<u>\$ (258)</u>	<u>\$ 109,588</u>	<u>\$ (226)</u>

Amortization expense related to amortizable intangible assets for the years ended December 27, 2018, December 28, 2017 and December 29, 2016, was \$32 thousand, \$32 thousand and \$32 thousand, respectively.

Estimated intangible asset amortization for the next five years is as follows (in thousands):

2019	\$ 32
2020	29
2021	—
2022	—
2023	—

## 6. Income Taxes

The components of the provision for income taxes are as follows (in thousands)

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
Current expense / (benefit):			
Federal	\$ 5,496	\$ (4,097)	\$ 14,588
State	1,669	479	2,422
Total current expense / benefit	<u>7,165</u>	<u>(3,618)</u>	<u>17,010</u>
Deferred expense / (benefit):			
Federal	922	(250)	(4,765)
State	(1,890)	(368)	(771)
Total deferred (benefit) / expense	<u>(968)</u>	<u>(618)</u>	<u>(5,536)</u>
Provision for income taxes	<u>\$ 6,197</u>	<u>\$ (4,236)</u>	<u>\$ 11,474</u>

The following is a summary of the differences between the total provision for income taxes as shown on the financial statements and the provision for income taxes that would result from applying the federal statutory tax rate of 21% for the year ended December 27, 2018 (35% for years ended December 28, 2017 and December 29, 2016) to income before income taxes (in thousands).

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
Computed “expected” provision at statutory rate	\$ 25,700	\$ 34,499	\$ 19,080
State income taxes, net of federal income tax benefit	(627)	(28)	1,073
Permanent differences:			
Excess tax benefit related to options exercised	(17,478)	(20,762)	—
Non-qualified option holder dividend equivalent	—	—	(7,877)
Other	457	691	(4)
Total permanent differences	(17,021)	(20,071)	(7,881)
Change in U.S. tax rate	(573)	(17,850)	—
Provision to return	(739)	(63)	(236)
Federal tax credits	(685)	(577)	(413)
Other, net	142	(146)	(149)
Provision for income taxes	<u>\$ 6,197</u>	<u>\$ (4,236)</u>	<u>\$ 11,474</u>

The permanent differences of \$17,478 thousand and \$20,762 thousand in fiscal 2018 and fiscal 2017, respectively, are the federal benefits due to the recognition of excess tax deductions for stock options exercised. In the table above, the 2018 and 2017 state benefits related to the recognition of excess tax benefits of \$3.3 million and \$1.0 million, respectively, are included in state income taxes, net of federal income tax benefit.

The Tax Cuts and Jobs Act (the “Act”), which was enacted on December 22, 2017, reduced the U.S. federal corporate income tax rate from 35% to 21% and created new taxes that may apply on certain foreign sourced earnings. As of December 28, 2017, we had not yet completed our accounting for the enactment-date income tax effects of the Act under ASC 740 for the remeasurement of deferred tax assets and liabilities and tax on global intangible low-tax income.

In 2017 and the first nine months of 2018, we recorded provisional amounts for certain enactment-date effects of the Act by applying the guidance in Staff Accounting Bulletin No. 118 (“SAB 118”). As of December 28, 2017, we remeasured certain deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future, which is generally 21%, and recorded a provisional amount of \$17.9 million. Upon further analysis of certain aspects of the Act and refinement of our calculations prior to the end of the measurement period and during the twelve months ended December 27, 2018, we completed our accounting for all the enactment-date income tax effects of the Act and adjusted our provisional amount by an additional \$600 thousand, which was included as a component of income tax expense from continuous operations. The changes to 2017 enactment-date provisional amounts decreased the effective tax rate for the year ended December 27, 2018 by 0.47%.

The Act also subjects a U.S. shareholder to tax on global intangible low-taxed income (“GILTI”) earned by certain foreign subsidiaries. The FASB Staff Q&A, Topic 740, No. 5, Accounting for Global Intangible Low-Taxed Income, states that an entity can make an accounting policy election to either recognize deferred taxes for temporary basis differences expected to reverse as GILTI in future years or provide for the tax expense related to GILTI in the year the tax is incurred. We have elected to recognize the resulting tax on GILTI as a period expense in the period the tax is incurred. However, we did not incur tax for the period ended December 27, 2018.

The tax effects of temporary differences that give rise to significant portions of the deferred income tax assets and (liabilities) are presented below (in thousands):

	Year Ended December 27, 2018	Year Ended December 28, 2017
<b>Deferred tax assets:</b>		
Accruals not currently deductible for tax purposes	\$ 13,338	\$ 8,993
Tenant improvement allowances	9,239	6,597
Inventories	3,948	4,111
Stock based compensation	3,684	3,108
Other intangibles	361	405
Gift card liability	242	648
Litigation accrual	172	583
Other	2,858	846
<b>Total deferred tax assets</b>	<b>33,842</b>	<b>25,291</b>
<b>Deferred tax liabilities:</b>		
Intangible assets	(27,023)	(26,868)
Fixed assets	(30,681)	(24,225)
Other	(2,976)	(1,416)
<b>Total deferred tax liabilities</b>	<b>(60,680)</b>	<b>(52,509)</b>
<b>Net deferred tax liabilities</b>	<b>\$ (26,838)</b>	<b>\$ (27,218)</b>

The Company generated \$776 thousand of state net operating losses in fiscal 2018, resulting in a total of \$2.2 million state net operating losses available to reduce future income taxes. The state net operating losses expire in various amounts beginning in 2032.

In assessing the realization of deferred tax assets, including net operating losses, management considered whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers taxable income in prior carryback periods, future reversals of existing taxable temporary differences, tax planning strategies, and future taxable income exclusive of reversing temporary differences and carryforwards in making this assessment, and accordingly, has concluded that no valuation allowance is necessary as of December 27, 2018 or December 28, 2017.

The Company files income tax returns with the U.S. Federal government and various state jurisdictions. Prior tax years beginning in year 2015 remain open to examination by the Internal Revenue Service. As of December 27, 2018, December 28, 2017, and December 29, 2016 the Company had unrecognized tax benefits of \$0, \$0, and \$0, respectively. These unrecognized tax benefits as of December 27, 2018, December 28, 2017, and December 29, 2016 would have no impact on the effective tax rate, if recognized. The Company's policy is to classify interest and penalties related to unrecognized tax benefits in income tax expense.

## 7. Fair Value Measurements

The Company estimates fair values in accordance with ASC 820, *Fair Value Measurement*. ASC 820 provides a framework for measuring fair value and expands disclosures required about fair value measurements. ASC 820 defines fair value as the price that would be received from the sale of an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. Additionally, ASC 820 defines levels within a hierarchy based upon observable and non-observable inputs.

- Level 1—Inputs that are quoted prices in active markets for identical assets or liabilities
- Level 2—Inputs other than quoted prices in active markets for assets or liabilities that are either directly or indirectly observable
- Level 3—Inputs that are non-observable that reflect the reporting entity's own assumptions

**Assets (Liabilities) Measured at Fair Value on a Recurring Basis**

(in thousands)	As of December 27, 2018	Level 1	Level 2	Level 3
<i>Designated as hedges:</i>				
Interest rate cap (cash flow hedge)	\$ 1,076	\$ —	\$ 1,076	\$ —
<i>Not designated as hedges:</i>				
Interest rate cap	\$ 1,075	\$ —	\$ 1,075	\$ —

(in thousands)	As of December 28, 2017	Level 1	Level 2	Level 3
<i>Designated as hedges:</i>				
Interest rate cap (cash flow hedge)	\$ 710	\$ —	\$ 710	\$ —
<i>Not designated as hedges:</i>				
Interest rate cap	\$ 710	\$ —	\$ 710	\$ —

Our derivative contracts are negotiated with counterparties without going through a public exchange. Accordingly, our fair value assessments give consideration to the risk of counterparty default (as well as our own credit risk). Our interest rate derivatives consist of interest rate cap contracts and are valued primarily based on data readily observable in public markets.

**8. Derivatives and Risk Management**

Changes in interest rates impact our results of operations. In an effort to manage our exposure to this risk, we enter into derivative contracts and may adjust our derivative portfolio as market conditions change.

***Designated as Cash Flow Hedge***

For derivative contracts designated as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of Accumulated Other Comprehensive Income (“AOCI”) and reclassified into earnings in the same period in which the hedged transaction affects earnings. The effective portion of the derivative represents the change in fair value of the hedge that offsets the change in fair value of the hedged item. To the extent the change in the fair value of the hedge does not perfectly offset the change in the fair value of the hedged item, the ineffective portion of the hedge is immediately recognized in earnings.

***Not Designated as Accounting Hedge***

For derivative contracts de-designated as accounting hedges, the change in the fair value is reflected through earnings. These changes in fair value are mark-to-market adjustments (“MTM adjustments”). MTM adjustments are defined as fair value changes recorded in periods other than the settlement period. Such fair value changes are not necessarily indicative of the actual settlement value of the underlying hedge in the contract settlement period. The AOCI related to the interest rate cap prior to the de-designation is being amortized over the remaining maturity period.

***Derivative Position as of December 27, 2018:***

(in thousands)	Notional Balance		Final Maturity Date	Other Assets	AOCI, Net of Tax
<i>Designated as hedges:</i>					
Interest rate cap (cash flow hedge)	\$ 102,500	U.S. dollars	December 2021	\$ 1,076	\$ 177
<i>Not designated as hedges:</i>					
Interest rate cap	\$ 102,500	U.S. dollars	December 2021	\$ 1,075	\$ 9

**Derivative Position as of December 28, 2017:**

(in thousands)	Notional Balance		Final Maturity Date	Other Assets	AOI, Net of Tax
<i>Designated as hedges:</i>					
Interest rate cap (cash flow hedge)	\$ 102,500	U.S. dollars	December 2021	\$ 710	\$ (133)
<i>Not designated as hedges:</i>					
Interest rate cap	\$ 102,500	U.S. dollars	December 2021	\$ 710	\$ (72)

**Designated Hedge Gain (Losses)**

Gains (losses) related to our designated hedge contracts are as follows:

(in thousands)	Effective Portion Reclassified From AOCI to Earnings			Effective Portion Recognized in Other Comprehensive Income (Loss)		
	Year Ended			Year Ended		
	December 27, 2018	December 28, 2017	December 29, 2016	December 27, 2018	December 28, 2017	December 29, 2016
Interest rate cap (cash flow hedge)	\$ —	\$ —	\$ —	\$ 391	\$ (381)	\$ 176
Interest rate swaps (cash flow hedges)	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 100

**Interest Rate Risk**

Our exposure to market risk from adverse changes in interest rates is primarily associated with our long-term debt obligations, which carry variable interest rates. Market risk associated with our variable interest rate long-term debt relates to the potential reduction in fair value and negative impact to future earnings, respectively, from an increase in interest rates.

In an effort to manage our exposure to the risk associated with our variable interest rate long term debt, we periodically enter into interest rate derivative contracts. We designate interest rate derivative contracts used to convert the interest rate exposure on a portion of our debt portfolio from a floating rate to a capped rate as cash flow hedges.

**Credit Risk**

To manage credit risk associated with our interest rate hedging program, we select counterparties based on their credit ratings and limit our exposure to any one counterparty.

The counterparties to our derivative contracts are financial institutions with investment grade credit ratings. To manage our credit risk related to our derivative financial instruments, we periodically monitor the credit risk of our counterparties, limit our exposure in the aggregate and to any single counterparty, and adjust our hedging position, as appropriate. The impact of credit risk, as well as the ability of each party to fulfill its obligations under our derivative financial instruments, is considered in determining the fair value of the contracts. Credit risk has not had a significant effect on the fair value of our derivative contracts. We do not have any credit risk-related contingent features or collateral requirements with our derivative financial instruments.

**9. Commitments and Contingencies**

**Lease Commitments**

The Company leases its corporate office, retail locations and distribution centers under long-term operating lease agreements that expire in various years through 2032. Additionally, certain equipment is leased under short-term operating leases.

Certain lease agreements include escalating rents over the lease terms. The Company expenses rent on a straight-line basis over the life of the lease, which commences on the date the Company has the right to control the property. The cumulative expense recognized on a straight-line basis in excess of the cumulative payments is included in deferred rent in the accompanying

Consolidated Balance Sheets. Future minimum lease payments under non-cancelable operating leases (with initial or remaining lease terms in excess of one year) as of December 27, 2018, are:

(in thousands)	Amount
2019	\$ 114,076
2020	131,394
2021	123,249
2022	116,925
2023	112,430
Thereafter	710,643
<b>Total minimum lease payments</b>	<b>\$ 1,308,717</b>

Lease expense for the years ended December 27, 2018, December 28, 2017, and December 29, 2016, was approximately \$94,103 thousand, \$71,524 thousand, and \$53,899 thousand, respectively.

**Litigation**

The Company is subject to other various legal actions, claims and proceedings arising in the ordinary course of business, including claims related to breach of contracts, products liabilities, intellectual property matters and employment related matters resulting from its business activities. The Company establishes reserves for specific legal proceedings when it determines that the likelihood of an unfavorable outcome is probable and the amount of loss can be reasonably estimated. These proceedings are not expected to have a material impact on the Company's Consolidated Financial Statements.

**10. Debt**

The following table summarizes our long-term debt as of December 27, 2018 and December 28, 2017 (dollars in thousands):

	Maturity Date	Interest Rate Per Annum at December 27, 2018	December 27, 2018	December 28, 2017
<b>Credit Facilities:</b>				
UBS Facility Term Loan B	September 30, 2023	4.48 % Variable	\$ 149,000	\$ 152,500
Wells Facility Revolving Line of Credit	September 30, 2021	3.72 % Variable	—	41,000
Total secured debt			149,000	193,500
Less: current maturities			3,500	3,500
Long-term debt maturities			145,500	190,000
Less: unamortized discount and debt issuance costs			3,666	4,438
Total long-term debt			<b>\$ 141,834</b>	<b>\$ 185,562</b>

**Repayment of Debt with Proceeds from Initial Public Offering**

On May 2, 2017, the Company completed its IPO, pursuant to which it sold an aggregate of 10,147,025 shares of Class A common stock, par value \$0.001 per share (after giving effect to the underwriters' exercise in full of their option to purchase additional shares) at a price of \$21.00 per share. The Company received aggregate net proceeds of approximately \$192.0 million after deducting underwriting discounts and commissions and other offering expenses.

The Company used net proceeds from the IPO of approximately \$192.0 million to repay a portion of the amounts outstanding under the Term Loan Facility, including accrued and unpaid interest. The partial paydown resulted in a loss on extinguishment of debt in the amount of approximately \$5.4 million related to unamortized original issue discount and unamortized deferred debt issuance costs.



**Dividend**

On September 30, 2016, the board of directors declared the Special Dividend and authorized the Option Payments. Payment of the Special Dividend and the Option Payments was made on September 30, 2016 to all stockholders and option holders of record at the close of business on September 30, 2016. In connection with the dividend, the Company refinanced its existing indebtedness by amending the prior asset-based revolving credit facility with an amended and restated \$200.0 million asset-based revolving credit facility maturing on September 30, 2021 (the “ABL Facility”), entering into a \$350.0 million senior secured term loan facility maturing on September 30, 2023 (the “Term Loan Facility” and together with the ABL Facility, our “Credit Facilities”) and repaying and terminating the prior term loan facility and the prior senior secured term loan facility with GCI Capital Markets LLC (the “GCI Facility”). As a result of the refinancing, the Company recorded \$162 thousand of loss on extinguishment of debt related to unamortized deferred debt issuance cost for the Company’s prior asset-based revolving credit facility, as well as recorded \$1,319 thousand of loss on extinguishment of debt related to unamortized original issue discount and unamortized deferred debt issuance cost for the prior term loan facility and GCI Facility. In addition, the Company recorded \$10,347 thousand of original issue discount and deferred debt issuance cost related to new third-party fees associated with the refinancing.

**Term Loan Facility**

As of December 27, 2018, the Term Loan Facility had an outstanding balance of \$149.0 million and requires quarterly repayments of \$875 thousand, which commenced on December 31, 2016, with the remainder due and payable at maturity. The Term Loan Facility matures on September 30, 2023.

As of December 27, 2018, the Term Loan Facility bore interest based on one of the following rates, at the Company’s option:

- i) Adjusted LIBOR Rate plus a margin of 2.50%
- ii) Base Rate plus a margin of 1.50%. Base Rate defined as the greater of the following:
  - (a) the base rate in effect on such day,
  - (b) the federal funds rate plus 0.50%,
  - (c) the adjusted LIBOR rate for the interest period of one month plus a margin of 1.00%

**ABL Facility**

As of December 27, 2018, the ABL Facility had a maximum availability of \$300 million with actual available borrowings limited to the sum, at the time of calculation, of eligible credit card receivables, plus the cost of eligible inventory, net of inventory reserves, multiplied by the product of an appraisal percentage multiplied by the appraised value of eligible inventory, plus 85% of eligible net trade receivables, plus all eligible cash on hand minus certain Availability Reserves (as defined in the credit agreement governing the ABL Facility). The ABL Facility is available for issuance of letters of credit and contains \$30.0 million for standby letters of credit and commercial letters of credit. Available borrowings under the facility are reduced by the face amount of outstanding letters of credit. The ABL Facility matures on September 30, 2021. As of December 27, 2018, the borrowings bear interest at a floating rate, which is based on one of the following rates at the option of the Company:

- i) LIBOR Rate plus a margin percentage ranging from 1.25% to 1.50% based on the level of borrowings or
- ii) Base Rate plus a margin (ranging from 0.25% to 0.50% based on the level of borrowings). The Base Rate is defined as the highest of the following:
  - (a) the federal funds rate plus 0.50%,
  - (b) Adjusted LIBOR Rate plus 1.00%, or
  - (c) the lender’s prime rate

As of December 27, 2018, the Company had net availability under the ABL Facility of \$289,141 thousand, including outstanding letters of credit of \$10,859 thousand.

The following table summarizes scheduled maturities of our debt, including current maturities, as of December 27, 2018 (in thousands):

	<b>Amount</b>
2019	\$ 3,500
2020	4,375
2021	2,625
2022	3,500
2023	135,000
Thereafter	—
<b>Total minimum debt payments</b>	<b>\$ 149,000</b>

**Covenants**

The credit agreements governing our Credit Facilities contain customary restrictive covenants that, among other things and with certain exceptions, limit the ability of the Company to (i) incur additional indebtedness and liens in connection therewith; (ii) pay dividends and make certain other restricted payments; (iii) effect mergers or consolidations; (iv) enter into transactions with affiliates; (v) sell or dispose of property or assets and (vi) engage in unrelated lines of business. In addition, these credit agreements subject us to certain reporting obligations and require that we satisfy certain financial covenants, including, among other things:

- a requirement that if borrowings under the ABL Facility exceed 90% of availability, we will maintain a certain fixed charge coverage ratio (defined as consolidated EBITDA less non-financed capital expenditures and income taxes paid to consolidated fixed charges, in each case as more fully defined in the credit agreement governing the ABL Facility).

The Term Loan Facility has no financial maintenance covenants. As of December 27, 2018, we were in compliance with the covenants of the Credit Facilities.

**Deferred Debt Issuance Cost and Original Issue Discount**

Deferred debt issuance cost related to our ABL Facility and our prior asset-based revolving credit facility of \$902 thousand and \$1005 thousand as of December 27, 2018 and December 28, 2017, respectively, are included in Other assets on our Consolidated Balance Sheets. Deferred debt issuance cost and original issue discount related to our Term Loan Facility of \$3,666 thousand as of December 27, 2018 and \$4,438 thousand as of December 28, 2017 are included in Term loans on our Consolidated Balance Sheets. Amortization expense was \$1,045 thousand, \$1,205 thousand, and \$954 thousand for the years ended December 27, 2018, December 28, 2017, and December 29, 2016.

**Fair Value of Debt**

Market risk associated with our fixed and variable rate long-term debt relates to the potential change in fair value and negative impact to future earnings, respectively, from a change in interest rates. The aggregate fair value of debt was based primarily on discounted cash flows utilizing estimated interest rates, maturities, credit risk, and underlying collateral and is classified primarily as Level 3 within the fair value hierarchy. At December 27, 2018 and December 28, 2017, the fair values of the Company's debt are as follows (in thousands):

<b>(in thousands)</b>	<b>December 27, 2018</b>	<b>December 28, 2017</b>
Total debt at par value	\$ 149,000	\$ 193,500
Less: unamortized discount and debt issuance costs	3,666	4,438
<b>Net carrying amount</b>	<b>\$ 145,334</b>	<b>\$ 189,062</b>
Fair value	\$ 147,883	\$ 193,881

## **11. Stockholders' Equity**

### ***Common Stock***

The Company has three classes of common stock: Class A, Class B and Class C. The holders of Class A common stock, Class B common stock and Class C common stock are entitled to share equally, on a per share basis, in dividends or other distributions. Class A common stockholders are entitled to one vote per share held. Class B and Class C common stockholders have no voting rights, except as otherwise provided by law. In the event of the voluntary liquidation or dissolution of the Company, each class of stock will share equally, on a per share basis, in all the assets of the Company that are available for distribution to stockholders.

### ***Conversion Features***

On May 2, 2017, all of the Class B common stock outstanding shares, upon completion of our initial public offering, were converted to Class A common stock.

Shares of Class C common stock may be converted, upon the election of holders of such shares of Class C common stock, into the same number of shares of Class A common stock under certain circumstances as provided in the Company's certificate of incorporation.

On July 26, 2017, all of the Class C common stock outstanding shares, upon the election of holders of such shares of Class C common stock, were converted to Class A common stock.

### ***Stock Incentive Plans***

On January 13, 2011, the Company adopted the 2011 Stock Option Plan (as amended, restated, supplemented or otherwise modified from time to time, the "2011 Plan") to provide for the grant of stock options to employees (including officers), consultants and non-employee directors of the Company and its subsidiaries. Pursuant to the terms of the 2011 Plan, the Company was authorized to grant options for the purchase of up to 12,520,407 shares as of December 29, 2016 and 10,780,970 shares as of December 31, 2015. As of December 29, 2016 and December 31, 2015, there were 179,575 and 104,269 shares available for grant pursuant to awards under the 2011 Plan, respectively.

We ceased granting awards under the 2011 Plan upon the implementation of the 2017 Plan, described below.

On April 13, 2017, the board of directors approved the Floor & Decor Holdings, Inc. 2017 Stock Incentive Plan (the "2017 Plan"), which was subsequently approved by the Company's stockholders. The 2017 Plan authorizes the Company to grant options and restricted stock awards to eligible employees (including officers), consultants and non-employee directors up to an aggregate of 5,000,000 shares of Class A common stock. In connection with the IPO, the Company granted options to purchase an aggregate of 1,254,465 shares of our Class A common stock to certain of our eligible employees and 15,475 shares of restricted stock to certain of our non-employee directors, in each case pursuant to the 2017 Plan and based on the public offering price of \$21.00 per share. As of December 27, 2018 and December 28, 2017, there were 2,850,768 and 3,690,255 shares available for grant pursuant to awards under the 2017 Plan, respectively.

### ***Secondary Offerings***

On July 25, 2017, certain of the Company's stockholders completed a secondary public offering (the "July Secondary Offering") of an aggregate of 10,718,550 shares of common stock at a price to the public of \$40.00 per share. The Company did not sell any shares in the July Secondary Offering and did not receive any proceeds from the sales of shares by the selling stockholders.

On November 20, 2017, certain of the Company's stockholders completed a secondary public offering (the "November Secondary Offering") of an aggregate of 7,475,000 shares of common stock at a price to the public of \$36.00 per share. The Company did not sell any shares in the November Secondary Offering and did not receive any proceeds from the sales of shares by the selling stockholders.

On May 29, 2018, certain of the Company’s stockholders completed a secondary public offering (the “May Secondary Offering”) of an aggregate of 10,000,000 shares of common stock at a price to the public of \$45.80 per share. The Company did not sell any shares in the May Secondary Offering and did not receive any proceeds from the sales of shares by the selling stockholders.

On September 14, 2018, certain of the Company’s stockholders completed a secondary public offering (the “September Secondary Offering”) of an aggregate of 11,500,000 shares of common stock at a price to the public of \$37.25 per share. The Company did not sell any shares in the September Secondary Offering and did not receive any proceeds from the sales of shares by the selling stockholders.

**Stock Options**

The Company accounts for stock-based compensation pursuant to ASC 718, *Compensation – Stock Compensation*, which requires measurement of compensation cost for all stock awards at fair value on the date of grant and recognition of compensation, net of forfeitures, over the requisite service period for awards expected to vest.

Stock options are granted with an exercise price greater than or equal to the fair market value on the date of grant, as authorized by the Company’s board of directors or compensation committee. Options granted have vesting provisions ranging from one to five years, and contractual terms of ten years. Stock option grants are generally subject to forfeiture if employment terminates prior to vesting.

The fair value of stock option awards granted was estimated using the Black-Scholes pricing model with the following weighted-average assumptions:

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
Risk-free interest rate	3.05 %	2.06 %	1.43 %
Expected volatility	42 %	39 %	40 %
Expected life (in years)	6.29	6.50	6.50
Dividend yield	— %	— %	— %

The Company estimates the volatility of the share price of its common stock by considering the historical volatility of the stock of similar public entities. In determining the appropriateness of the public entities included in the volatility assumption the Company considered a number of factors, including the entity’s life cycle stage, growth profile, size, financial leverage and products offered.

The table below summarizes the changes in all stock options for the following periods:

	Options	Weighted Average Exercise Price	Options Exercisable at End of Year	Weighted Average Exercise Price of Exercisable Options	Weighted Average Fair Value/Share of Options Granted During the Year
Outstanding at December 31, 2015	10,460,119	\$ 4.77	6,656,524	\$ 4.00	\$ —
Granted	2,025,535	9.94	—	—	4.13
Exercised	(145,140)	3.48	—	—	—
Forfeited or expired	(361,403)	6.65	—	—	—
Outstanding at December 29, 2016	11,979,111	5.34	8,151,056	4.20	—
Granted	1,339,668	21.68	—	—	9.20
Exercised	(1,828,339)	4.85	—	—	—
Forfeited or expired	(236,354)	9.17	—	—	—
Outstanding at December 28, 2017	11,254,086	7.28	7,448,532	4.52	—
Granted	926,775	34.07	—	—	15.63
Exercised	(2,069,195)	5.09	—	—	—
Forfeited or expired	(258,838)	13.12	—	—	—
Outstanding at December 27, 2018	9,852,828	\$ 10.11	6,409,257	\$ 5.21	\$ —

The intrinsic value for stock options is defined as the difference between the exercise price and the value of the Company's common stock (on a minority, non-marketable basis). The per share value of the Company's common stock as of December 27, 2018, was \$26.01. The intrinsic value of stock options exercised was \$87,151 thousand and \$62,508 thousand for the years ended December 27, 2018 and December 28, 2017, respectively. The aggregate intrinsic value of stock options outstanding as of December 27, 2018, was \$165,404 thousand with a weighted-average remaining contractual life of 5.3 years. The aggregate intrinsic value of stock options exercisable as of December 27, 2018, was \$133,485 thousand with a weighted-average remaining contractual life of 3.8 years. The Company's total unrecognized compensation cost related to stock options as of December 27, 2018, was \$26,135 thousand, which is expected to be recognized over a weighted average period of 3.5 years.

#### ***Restricted Stock***

During fiscal 2018, we granted 10,165 shares of restricted stock to certain of our non-employee directors. Restricted stock granted have vesting provisions ranging from two to four years, and the aggregate fair value of restricted stock outstanding as of December 27, 2018, was \$566 thousand. As of December 27, 2018, there were 21,775 shares of restricted stock outstanding. The Company's total unrecognized compensation cost related to restricted stock as of December 27, 2018, was \$489 thousand, which is expected to be recognized over a weighted average period of 2.0 years.

During fiscal 2017, we granted 15,475 shares of restricted stock to certain of our non-employee directors. Restricted stock granted had vesting provisions of four years, and the aggregate fair value of restricted stock outstanding as of December 28, 2017, was \$767 thousand. As of December 28, 2017, there were 15,475 shares of restricted stock outstanding. The Company's total unrecognized compensation cost related to restricted stock as of December 28, 2017, was \$270 thousand, which is expected to be recognized over a weighted average period of 3.3 years.

#### ***Employee Stock Purchase Plan***

At our 2018 annual meeting of stockholders held on May 17, 2018, our stockholders approved the Floor & Decor Holdings, Inc. Employee Stock Purchase Plan (the "ESPP"), which became available to substantially all of our employees beginning in the third quarter of fiscal 2018. The ESPP is a tax-qualified plan under Section 423 of the Internal Revenue Code, and it permits eligible employees to purchase shares of our common stock through payroll deductions, subject to certain limitations. The purchase price of the shares under the ESPP in no event will be less than the lesser of 85% of the lower of the fair market value of our common stock on either the first or last trading day of each six-month offering period. There are 1,500,000 shares of our Class A common stock, par value \$0.001 per share, approved for issuance under the ESPP. As of December 27, 2018, eligible employees contributed \$1.4 million to purchase shares, and during fiscal 2018, the Company recognized \$333 thousand of stock-based compensation expense related to the ESPP.

## **12. Earnings Per Share**

### **Net Income per Common Share**

We calculate basic earnings per share by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income by the weighted average number of common shares outstanding adjusted for the dilutive effect of stock options.

The following table shows the computation of basic and diluted earnings per share:

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
<b>(in thousands, except per share data)</b>			
Net income	\$ 116,187	\$ 102,788	\$ 43,039
Basic weighted average shares outstanding	96,770	90,951	83,432
Dilutive effect of share based awards	7,791	8,709	4,999
Diluted weighted average shares outstanding	104,561	99,660	88,431
Basic earnings per share	\$ 1.20	\$ 1.13	\$ 0.52
Diluted earnings per share	\$ 1.11	\$ 1.03	\$ 0.49

The following have been excluded from the computation of dilutive effect of share based awards because the effect would be anti-dilutive:

	Year Ended December 27, 2018	Year Ended December 28, 2017	Year Ended December 29, 2016
<b>(in thousands)</b>			
Stock options	298	849	2,004

### 13. Selected Quarterly Financial Information (unaudited)

The following tables present the Company's unaudited quarterly results for fiscal 2018 and fiscal 2017.

<b>(in thousands, except per share data)</b>	Fiscal 2018			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net sales	\$ 402,948	\$ 434,279	\$ 435,882	\$ 436,739
Gross profit	165,386	177,638	178,226	181,018
Income from continuing operations	36,506	37,245	34,237	23,313
Basic earnings from continuing operations per share	0.38	0.39	0.35	0.24
Diluted earnings from continuing operations per share	0.35	0.35	0.33	0.22
Net income	31,871	39,846	26,568	17,902
Basic earnings per share	0.33	0.41	0.27	0.18
Diluted earnings per share	0.30	0.38	0.25	0.17

<b>(in thousands, except per share data)</b>	Fiscal 2017			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net sales	\$ 307,296	\$ 344,047	\$ 343,923	\$ 389,501
Gross profit	125,471	142,228	142,491	162,374
Income from continuing operations	22,672	34,102	28,596	32,401
Basic earnings from continuing operations per share	0.27	0.38	0.30	0.34
Diluted earnings from continuing operations per share	0.26	0.34	0.28	0.31
Net income	11,128	20,429	23,255	47,976
Basic earnings per share	0.13	0.22	0.25	0.51
Diluted earnings per share	0.13	0.20	0.22	0.46

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

**ITEM 9A. CONTROLS AND PROCEDURES.**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this report. Disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in the reports that we file or submit under the Exchange Act has been appropriately recorded, processed, summarized and reported on a timely basis and are effective in ensuring that such information is accumulated and communicated to the Company’s management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 27, 2018, our disclosure controls and procedures were not effective due to a material weakness in internal control over financial reporting, described below.

**Management’s Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining an adequate system of internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act), pursuant to Rule 13a-15(c) of the Exchange Act. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

A company’s internal control over financial reporting includes policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company, (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company, and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness for future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, we assessed the effectiveness of our internal control over financial reporting as of December 27, 2018, using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control—Integrated Framework (2013). A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

We identified a material weakness in internal control related to ineffective ITGCs in the areas of user access and program change management over certain information technology systems and in the reports generated from these systems used in the execution of controls that support the Company’s financial reporting processes. Our business process controls (automated and manual) that are dependent on the affected ITGCs were also deemed ineffective because they could have been adversely impacted. We believe that these control deficiencies were a result of: information technology control processes lacking sufficient documentation and formality such that the successful operation of ITGCs was overly dependent upon knowledge and actions of certain individuals with information technology control expertise; insufficient training of information technology personnel on the importance of ITGCs; and risk-assessment processes inadequate to identify and assess changes in information technology environments that could impact internal control over financial reporting. The material weakness did not result in any identified misstatements to the financial statements, and there were no changes to previously released financial results. Based on this material weakness, the Company’s management concluded that at December 27, 2018, the Company’s internal control over financial reporting was not effective.

The Company's independent registered public accounting firm, Ernst & Young LLP has issued an adverse audit report on the effectiveness of the Company's internal control over financial reporting as of December 27, 2018, which appears in Item 8 of this Annual Report.

As a result of the identification of the material weakness, and prior to filing this Annual Report, we performed further analysis and completed additional procedures intended to ensure our consolidated financial statements for the year ended December 27, 2018 were prepared in accordance with GAAP. Based on these procedures and analysis, and notwithstanding the material weakness in our internal control over financial reporting, our management has concluded that our consolidated financial statements and related notes thereto included in this Annual Report have been prepared in accordance with GAAP. Our Chief Executive Officer and Chief Financial Officer have certified that, based on each such officer's knowledge, the financial statements, as well as the other financial information included in this Annual Report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this Annual Report. In addition, Ernst & Young LLP has issued an unqualified opinion on our financial statements, which is included in Item 8 of this Annual Report, and we have developed a remediation plan for the material weakness, which is described below.

#### **Remediation**

Our management has been implementing and continues to implement measures designed to ensure that control deficiencies contributing to the material weakness are remediated, such that these controls are designed, implemented, and operating effectively. The remediation actions include: (i) creating and filling an information technology compliance oversight function; (ii) developing a training program addressing ITGCs and policies, including educating control owners concerning the principles and requirements of each control, with a focus on those related to user access and change-management over information technology systems impacting financial reporting; (iii) developing and maintaining documentation underlying ITGCs to enhance control knowledge across the entire IT organization; (iv) developing enhanced risk assessment procedures and controls related to changes in information technology systems; (v) implementing an information technology management review and testing plan to monitor ITGCs with a specific focus on systems supporting our financial reporting processes; and (vi) enhanced quarterly reporting on the remediation measures to the Audit Committee of the Board.

We believe that these actions will remediate the material weakness. The weakness will not be considered remediated, however, until the applicable controls operate for a sufficient period of time and our management has concluded, through testing, that these controls are operating effectively. We expect that the remediation of this material weakness will be completed prior to the end of fiscal 2019.

#### **Changes in Internal Control over Financial Reporting**

Except for the material weakness identified above, as of December 27, 2018, there have been no other changes in our internal control over financial reporting (as defined in Rules 13a-15(f) or 15d-15(f) of the Exchange Act) during our fourth quarter ended December 27, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### **ITEM 9B. OTHER INFORMATION .**

None.



**PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE .**

The information required by this Item will be contained in our definitive Proxy Statement in connection with our 2018 Annual Meeting of Stockholders, which will be filed with the SEC within 120 days after the end of our fiscal year ended December 27, 2018 (the “Proxy Statement”), and is incorporated herein by reference.

**ITEM 11. EXECUTIVE COMPENSATION .**

The information required by this Item will be set forth in the Proxy Statement and is incorporated herein by reference, under the captions “Director Compensation,” “Executive Compensation” and “Compensation Discussion and Analysis;” provided, however, that the subsection entitled “Executive Compensation—Compensation Committee Report” shall not be deemed to be incorporated by reference.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS .**

The information required by this Item will be set forth in the Proxy Statement and is incorporated herein by reference, under the caption “Certain Beneficial Owners.”

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE .**

The information required by this Item will be set forth in the Proxy Statement and is incorporated herein by reference, under the captions “Certain Relationships and Related Transactions,” and “Other Board Information—Director Independence.”

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES .**

The Information required under this Item will be included in the Proxy Statement and is incorporated herein by reference, under the caption “Ratification of Appointment of Independent Registered Public Accounting Firm.”

**PART IV**

**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES .**

(a) **Documents filed as part of the Annual Report:**

1. **Financial Statements filed in Part II, Item 8 of this Annual Report:**

Report of Independent Registered Public Accounting Firm  
Consolidated Balance Sheets as of December 27, 2018 and December 28, 2017  
Consolidated Statements of Operations for the years ended December 27, 2018, December 28, 2017 and December 29, 2016  
Consolidated Statements of Comprehensive Income for the years ended December 27, 2018, December 28, 2017 and December 29, 2016  
Consolidated Statements of Cash Flows for the years ended December 27, 2018, December 28, 2017 and December 29, 2016  
Consolidated Statement of Changes in Shareholders' Equity for the years ended December 27, 2018, December 28, 2017 and December 29, 2016  
Notes to Consolidated Financial Statements

2. **Financial Statement Schedules:**

There are no Financial Statement Schedules included with this filing for the reason that they are not applicable or are not required or the information is included in the financial statements or notes thereto

3. **Exhibits:**

**Exhibit No.**

- 3.1 [Restated Certificate of Incorporation of Floor & Decor Holdings, Inc.\(1\)](#)
- 3.2 [Second Amended and Restated Bylaws of Floor & Decor Holdings, Inc.\(1\)](#)
- 4.1 [Specimen Class A Common Stock Certificate\(2\)](#)
- 4.2 [Registration Rights Agreement, dated May 2, 2017, by and among Floor & Decor Holdings, Inc., Ares Corporate Opportunities Fund III, L.P., FS Equity Partners VI, L.P. and the other stockholders party thereto\(3\)](#)
- 4.3 [Investor Rights Agreement, dated May 2, 2017, by and among Floor & Decor Holdings, Inc., Ares Corporate Opportunities Fund III, L.P., FS Equity Partners VI, L.P. and FS Affiliates VI, L.P.\(3\)](#)
- 10.1 [FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan\(4\)#](#)
- 10.2 [First Amendment to FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan\(4\)#](#)
- 10.3 [Second Amendment to FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan\(4\)#](#)
- 10.4 [Third Amendment to FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan\(4\)#](#)
- 10.5 [Fourth Amendment to FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan\(5\)#](#)
- 10.6 [Form of Stock Option Agreement under the FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan\(4\)](#)
- 10.7 [Floor & Decor Holdings, Inc. 2017 Stock Incentive Plan\(3\)#](#)
- 10.8 [Form of Stock Option Agreement under the Floor & Decor Holdings, Inc. 2017 Stock Incentive Plan\(2\)](#)
- 10.9 [Form of Restricted Stock Agreement under the Floor & Decor Holdings, Inc. 2017 Stock Incentive Plan\(4\)](#)
- 10.10 [Form of Indemnification Agreement by and between Floor & Decor Holdings, Inc. and its directors and officers\(4\)](#)
- 10.11 [Amended and Restated Employment Agreement, dated July 29, 2015, between FDO Holdings, Inc., Floor and Decor Outlets of America, Inc. and Thomas V. Taylor\(4\)#](#)
- 10.12 [Consulting Agreement, dated December 3, 2012, by and between Floor and Decor Outlets of America, Inc., FDO Holdings, Inc. and George Vincent West\(4\)#](#)
- 10.13 [Amended and Restated Employment Agreement, dated July 29, 2015, between FDO Holdings, Inc., Floor and Decor Outlets of America, Inc. and Lisa G. Laube\(4\)#](#)
- 10.14 [Amended and Restated Employment Agreement, dated July 29, 2015, between FDO Holdings, Inc., Floor and Decor Outlets of America, Inc. and Trevor S. Lang\(4\)#](#)
- 10.15 [Amended and Restated Employment Agreement, dated July 29, 2015, between FDO Holdings, Inc., Floor and Decor Outlets of America, Inc. and David V. Christopherson\(4\)#](#)
- 10.16 [Amended and Restated Employment Agreement, dated July 29, 2015, between FDO Holdings, Inc., Floor and Decor Outlets of America, Inc. and Brian K. Robbins\(4\)#](#)

10.17	<a href="#">Floor &amp; Decor Holdings, Inc Employee Stock Purchase Plan(6)#</a>
10.18	<a href="#">First Amendment to Floor &amp; Decor Holdings, Inc. Employee Stock Purchase Plan(7)#</a>
10.19	<a href="#">Second Amendment to Floor &amp; Decor Holdings, Inc. Employee Stock Purchase Plan(8)#</a>
10.20	<a href="#">Amended and Restated Credit Agreement, dated as of September 30, 2016, by and among Floor and Decor Outlets of America, Inc., FDO Acquisition Corp., Wells Fargo Bank, National Association, as Administrative Agent, Collateral Agent and Swing Line Lender, Wells Fargo Bank, National Association, as Term Loan Agent, the lenders from time to time party thereto, Bank of America, N.A., as Syndication Agent, and Wells Fargo Bank, National Association and Merrill Lynch, Pierce and Fenner &amp; Smith Incorporated, as Joint Lead Arrangers and Joint Bookrunners(4)</a>
10.21	<a href="#">Amended and Restated Security Agreement, dated as of September 30, 2016, by and among Floor and Decor Outlets of America, Inc., the other borrowers and guarantors party thereto from time to time, Wells Fargo Bank, National Association, as Collateral Agent, and Wells Fargo Bank, National Association, as Administrative Agent(4)</a>
10.22	<a href="#">Credit Agreement, dated as of September 30, 2016, by and among Floor and Decor Outlets of America, Inc., FDO Acquisition Corp., the lenders from time to time parties thereto, UBS AG, Stamford Branch, as Administrative Agent and Collateral Agent, and UBS Securities LLC, Merrill Lynch, Pierce, Fenner &amp; Smith Incorporated, Barclays Bank PLC, Goldman Sachs Bank USA and Wells Fargo Securities LLC, as Joint Lead Arrangers and Joint Bookrunners(4)</a>
10.23	<a href="#">Security Agreement, dated as of September 30, 2016, by and among Floor and Decor Outlets of America, Inc., FDO Acquisition Corp., the other loan parties from time to time party thereto and UBS AG, Stamford Branch, as Collateral Agent and Administrative Agent and the lenders party thereto(4)</a>
10.24	<a href="#">Guaranty Agreement, dated as of September 30, 2016, by FDO Acquisition Corp. in favor of UBS AG, Stamford Branch, as Collateral Agent, and UBS AG, Stamford Branch, as Administrative Agent and the lenders party thereto(4)</a>
10.25	<a href="#">Amendment No. 1 to Credit Agreement, dated as of March 31, 2017, by and among Floor and Decor Outlets of America, Inc., FDO Acquisition Corp., the other loan parties from time to time party thereto, the lenders from time to time party thereto, and UBS AG, Stamford Branch, as Administrative Agent and Collateral Agent(4)</a>
10.26	<a href="#">Amendment No. 2 to Credit Agreement, dated as of November 22, 2017, by and among Floor and Decor Outlets of America, Inc., FDO Acquisition Corp., the other loan parties from time to time party thereto, the lenders from time to time party thereto, and UBS AG, Stamford Branch, as Administrative Agent and Collateral Agent(9)</a>
21.1	<a href="#">List of subsidiaries(4)</a>
23.1	<a href="#">Consent of Ernst &amp; Young LLP, independent registered public accounting firm</a>
31.1	<a href="#">Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>
31.2	<a href="#">Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>
32.1	<a href="#">Certification of CEO and CFO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</a>
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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# Denotes a management contract or compensatory plan or arrangement.

- (1) Filed as an exhibit to Amendment No. 4 to the Registrant’s Registration Statement on Form S-1 (File No. 333-216000) filed with the SEC on April 24, 2017, and incorporated herein by reference.
- (2) Filed as an exhibit to Amendment No. 3 to the Registrant’s Registration Statement on Form S-1 (File No. 333-216000) filed with the SEC on April 17, 2017, and incorporated herein by reference.
- (3) Filed as an exhibit to the Registrant’s Form 8-K (File No. 001-38070) filed with the SEC on May 2, 2017, and incorporated herein by reference.
- (4) Filed as an exhibit to Amendment No. 2 to the Registrant’s Registration Statement on Form S-1 (File No. 333-216000) filed with the SEC on April 7, 2017, and incorporated herein by reference.

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- (5) Filed as an exhibit to the Registrant's Registration Statement on Form S-1 (File No. 333-221525) filed with the SEC on November 13, 2017, and incorporated herein by reference.
- (6) Filed as Annex A to the Registrant's Definitive Proxy Statement (File No. 001-38070), filed with the SEC on March 27, 2018, and incorporated herein by reference.
- (7) Filed as Exhibit 99.2 to the Registrant's Registration Statement on Form S-8 (File No. 333-225092), filed with the SEC on May 22, 2018, and incorporated herein by reference.
- (8) Filed as Exhibit 10.1 to the Registrant's Form 10-Q (File No. 001-38070) filed with the SEC on November 1, 2018, and incorporated herein by reference.
- (9) Filed as Exhibit 10.23 to the Registrant's Form 10-K (File No. 001-38070) filed with the SEC on March 5, 2018, and incorporated herein by reference.

**ITEM 16. FORM 10-K SUMMARY**

None.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**FLOOR & DECOR HOLDINGS, INC.**

Dated: February 25, 2019

/s/ Thomas V. Taylor  
Thomas V. Taylor  
*Chief Executive Officer*

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company and in the capacities indicated on the twenty-fifth day of February 2019.

<b>Signature</b>	<b>Title</b>	<b>Date</b>
<u>/s/ Thomas V. Taylor</u> Thomas V. Taylor	Chief Executive Officer (Principal Executive Officer) and Director	February 25, 2019
<u>/s/ Trevor S. Lang</u> Trevor S. Lang	Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	February 25, 2019
<u>/s/ Norman H. Axelrod</u> Norman H. Axelrod	Chairman of the Board	February 25, 2019
<u>/s/ George Vincent West</u> George Vincent West	Vice Chairman of the Board	February 25, 2019
<u>/s/ Brad J. Brutocao</u> Brad J. Brutocao	Director	February 25, 2019
<u>/s/ Michael Fung</u> Michael Fung	Director	February 25, 2019
<u>/s/ David B. Kaplan</u> David B. Kaplan	Director	February 25, 2019
<u>/s/ Rachel H. Lee</u> Rachel H. Lee	Director	February 25, 2019
<u>/s/ John M. Roth</u> John M. Roth	Director	February 25, 2019
<u>/s/ Peter M. Starrett</u> Peter M. Starrett	Director	February 25, 2019
<u>/s/ Richard L. Sullivan</u> Richard L. Sullivan	Director	February 25, 2019
<u>/s/ Felicia D. Thornton</u> Felicia D. Thornton	Director	February 25, 2019

We consent to the incorporation by reference in the following Registration Statements:

- (1) Registration Statement (Form S-8 No. 333-217474) pertaining to the Floor & Decor Holdings, Inc. 2017 Stock Incentive Plan & FDO Holdings, Inc. Amended and Restated 2011 Stock Incentive Plan, and
- (2) Registration Statement (Form S-8 No. 333-225092) pertaining to the Floor & Decor Holdings, Inc. Employee Stock Purchase Plan;

of our reports dated February 25, 2019, with respect to the consolidated financial statements of Floor & Decor Holdings, Inc. and the effectiveness of internal control over financial reporting of Floor & Decor Holdings, Inc., included in this Annual Report (Form 10-K) of Floor & Decor Holdings, Inc. for the year ended December 27, 2018.

/s/ Ernst & Young LLP

Atlanta, Georgia  
February 25, 2019

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**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
PURSUANT TO RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Thomas V. Taylor, certify that:

1. I have reviewed this annual report on Form 10-K of Floor & Decor Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 25, 2019

/s/ Thomas V. Taylor  
Thomas V. Taylor  
Chief Executive Officer  
(Principal Executive Officer)

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**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
PURSUANT TO RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Trevor S. Lang, certify that:

1. I have reviewed this annual report on Form 10-K of Floor & Decor Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 25, 2019

/s/ Trevor S. Lang  
Trevor S. Lang  
*Executive Vice President and Chief Financial Officer*  
*(Principal Financial Officer and Principal Accounting Officer)*

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**CERTIFICATIONS OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER**  
**PURSUANT TO 18 U.S.C. SECTION 1350,**  
**AS ADOPTED PURSUANT TO**  
**SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the annual report on Form 10-K of Floor & Decor Holdings, Inc. (the "Company"), for the fiscal year ended December 27, 2018, as filed with the Securities and Exchange Commission (the "SEC") on the date hereof (the "Periodic Report"), Thomas V. Taylor, as Chief Executive Officer of the Company, and Trevor S. Lang, as Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002 ("Section 906"), that, to the best of his knowledge:

1. The Periodic Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. §78m or 78o(d)); and
2. The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 25, 2019

/s/ Thomas V. Taylor  
Thomas V. Taylor  
*Chief Executive Officer*  
*(Principal Executive Officer)*

Dated: February 25, 2019

/s/ Trevor S. Lang  
Trevor S. Lang  
*Executive Vice President and Chief Financial Officer*  
*(Principal Financial Officer and Principal Accounting Officer)*

A signed original of this written statement as required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signatures that appear in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

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